

Applying IFRS

IFRS 11 Joint Arrangements

Challenges in adopting and applying IFRS 11

June 2014

The EY logo is positioned in the bottom left corner of the page. It consists of the letters 'EY' in a bold, white, sans-serif font. The background of the entire page is a blurred office scene with two men in business attire looking at documents. A large yellow diagonal shape cuts across the lower right portion of the image. In the foreground, there are various office items like a desk, a pen, and a roll of paper.

EY

Building a better
working world

Contents

In this issue:

Introduction	2
1. Overview	3
2. Scope	5
2.1 Application by venture capital organisations.....	5
2.2 Application to joint ventures held for sale.....	5
3. Joint arrangements	6
3.1 Unit of account	7
4. Joint control	10
4.1 Relevant activities in a joint arrangement.....	11
4.2 Rights to control collectively.....	12
4.3 Unanimous consent.....	16
4.4 Other practical issues with assessing joint control.....	19
5. Classification of a joint arrangement.....	21
5.1 Separate vehicle	23
5.2 Legal form of the separate vehicle	24
5.3 Contractual terms.....	24
5.4 Other facts and circumstances.....	27
6. Accounting for joint operations	32
6.1 Difference from proportionate consolidation	33
6.2 Determining the relevant IFRS	35
6.3 Parties to a joint operation without joint control	35
6.4 Joint operations with a non-controlling interest/passive investor.....	36
6.5 Transactions between a joint operator and a joint operation.....	37
7. Accounting for joint ventures	38
7.1 Interest in a joint venture without joint control	38
7.2 Contributions of non-monetary assets to a joint venture	38
8. Continuous assessment	39
8.1 When to reassess under IFRS 11	39
8.2 Changes in ownership with respect to a joint venture	39
8.3 Changes in ownership with respect to a joint operation	43
8.4 Changes from a joint operation to a joint venture.....	45
9. Disclosures	46
9.1 Principles of IFRS 12.....	46
9.2 Disclosing judgements.....	46
9.3 Nature of an entity's interest in a joint arrangement	47
9.4 Nature, extent and financial effects of an entity's interest in a joint venture.....	47
9.5 Risks associated with interests in joint ventures.....	53
9.6 Joint arrangements that are structured entities.....	54
9.7 Related party transactions	55
Appendix – Defined terms	59

Introduction

In May 2011, the International Accounting Standards Board (IASB) issued three standards: IFRS 10 *Consolidated Financial Statements*, IFRS 11 *Joint Arrangements* and IFRS 12 *Disclosure of Interests in Other Entities*. These standards are effective for annual periods beginning on or after 1 January 2013, and are applied retrospectively (with some transition reliefs).

IFRS 11 replaced IAS 31 *Interests in Joint Ventures* and SIC-13 *Jointly-controlled Entities – Non-monetary Contributions by Venturers*. IFRS 11 defines two types of joint arrangement (joint operations and joint ventures) and specifies the accounting for each arrangement. The option previously available under IAS 31 to account for jointly controlled entities using proportionate consolidation is no longer available.

All of the disclosure requirements for joint arrangements are included in IFRS 12. IFRS 12 requires disclosure of judgements made to determine whether an entity has joint control over another entity and the judgements made to classify joint arrangements. An entity is also required to disclose summarised financial information for each material joint venture.

This publication describes the requirements of IFRS 11, explores application issues related to IFRS 11, and summarises the related disclosure requirements for joint arrangements. Because IFRS 11 uses the principle of control in IFRS 10 to define joint control, reference to our publication, *Applying IFRS - IFRS 10 Consolidated Financial Statements: Challenges in adopting and applying IFRS 10* may be helpful in assessing whether there is joint control. This publication addresses some of the key practice issues from implementing IFRS 11 based on experiences of applying it during 2013.

June 2014

1. Overview

There are many reasons why entities might use a joint arrangement to conduct business, such as to:

- ▶ Accelerate the development of new technologies
- ▶ Turn existing technologies into marketable products
- ▶ Enter new markets or industries
- ▶ Expand geographically
- ▶ Protect supply chain and production capacity
- ▶ Leverage intellectual property held by others (including competitors)
- ▶ Distribute risk
- ▶ Provide an alternative to raising bank or equity financing
- ▶ Access additional expertise
- ▶ Comply with the requirements of a government stakeholder
- ▶ Facilitate distribution of products
- ▶ Take the first step in acquiring a business

As discussed in more detail below, IFRS 11 covers all arrangements in which there is joint control, regardless of the terminology used to describe the arrangement. Management will need to carefully evaluate the terms of an arrangement, and the relevant facts and circumstances, to determine if it qualifies as a joint arrangement.

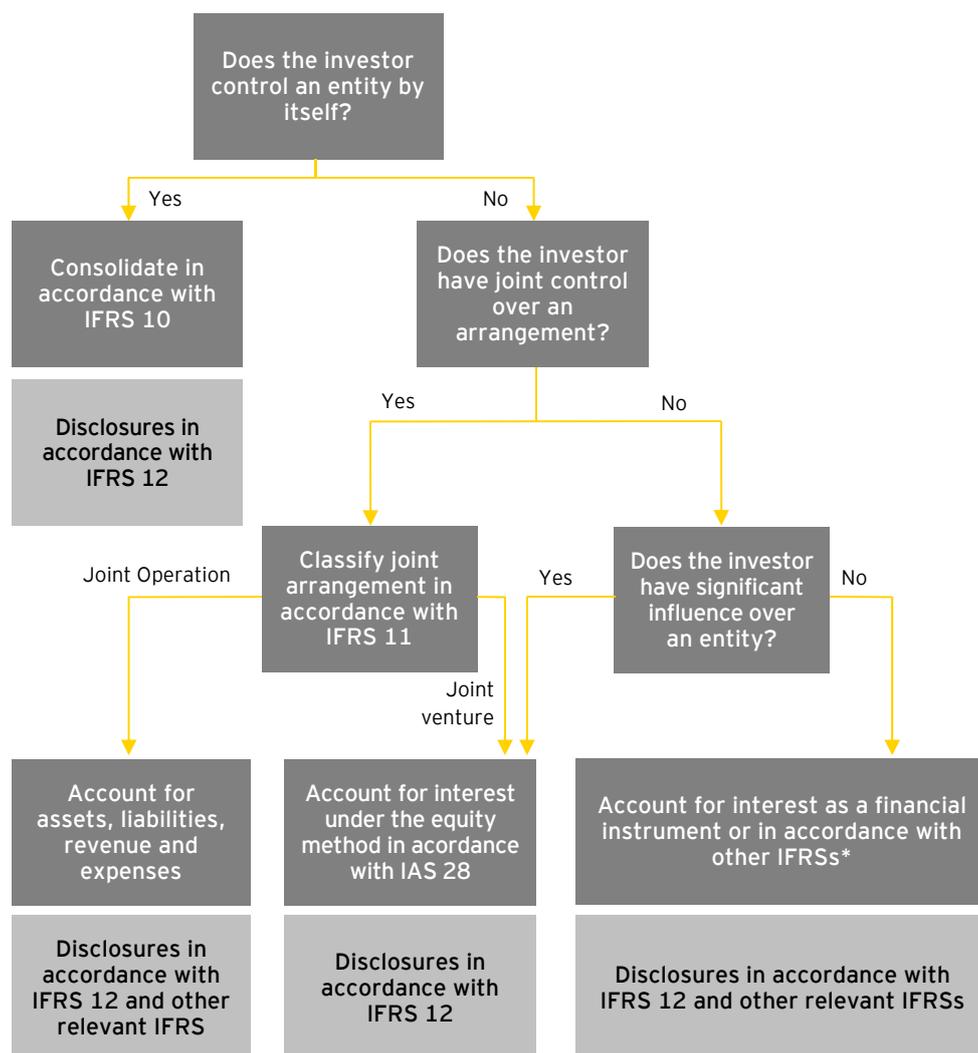
Excerpts from IFRS 11

- | | |
|---|---|
| 4 | A joint arrangement is an arrangement of which two or more parties have joint control. |
| 5 | A joint arrangement has the following characteristics:
(a) The parties are bound by a contractual arrangement.
(b) The contractual arrangement gives two or more of those parties joint control of the arrangement. |
| 6 | A joint arrangement is either a <i>joint operation</i> or a <i>joint venture</i> . |
| 7 | Joint control is the contractually agreed sharing of control of an arrangement, which exists only when decisions about the relevant activities require the unanimous consent of the parties sharing control. |

We explore the definition of joint control and the concept of a joint arrangement in more detail in Sections 4 and 5, respectively. In Sections 6 and 7, we describe the two types of joint arrangements defined in IFRS 11, joint operations and joint ventures, and explain how to classify a joint arrangement as one or the other. We also discuss in Section 6 the importance of considering the rights and obligations in the context of the normal course of business when classifying a joint arrangement.

Diagram 1 summarises the definitions and accounting for each type of joint arrangement, as well as the interaction between IFRS 10, IFRS 11, IFRS 12 and IAS 28 *Investments in Associates and Joint Ventures*. The accounting for joint ventures is discussed in further detail in Section 7.

Diagram 1 – Interaction between IFRS 10, IFRS 11, IFRS 12 and IAS 28



* This would be the case, for example, if an entity has control over (or simply rights to) assets and obligations for liabilities, that is not a separate entity. In this case, the entity would account for these assets and obligations in accordance with the relevant IFRS (as discussed in Section 6).

This publication does not address the accounting for joint ventures or joint operations in separate financial statements, although IFRS 11 does address this topic for joint operations. During 2013, the IFRS Interpretations Committee (IC) received a number of requests for further guidance on the application of IFRS 11. Where the IC has addressed particular issues, we have included summaries of the discussions in this publication. However, the IC will continue to discuss a number of implementation issues during 2014 and we encourage readers to carefully monitor those meetings for the latest developments, as required.

2. Scope

IFRS 11 applies to all entities that are party to a joint arrangement.

The scope of IFRS 11 was intended to be generally the same as IAS 31: the scope of IFRS 11 is limited to arrangements where there is joint control. However, since the definition IFRS 11's concept of joint control refers to IFRS 10's definition of control, which is broader than the notion of control under IAS 27 *Consolidated and Separate Financial Statements*, there may be more arrangements that qualify as joint arrangements under IFRS 11.

2.1 Application by venture capital organisations

IFRS 11 applies to all entities that are a party to a joint arrangement, including venture capital organisations, mutual funds, unit trusts, investment-linked insurance funds and similar entities (referred to hereafter as venture capital organisations).

However, venture capital organisations can choose to measure investments in joint ventures at fair value under IAS 28 *Investments in Associates*. To utilise the exemption, the venture capital organisation elects to measure the investment in a joint venture at fair value through profit or loss in accordance with IFRS 9 *Financial Instruments* (or IAS 39 *Financial Instruments: Recognition and Measurement*).

Venture capital organisations are subject to the disclosure requirements of IFRS 12 (see Section 9).

2.2 Application to joint ventures held for sale

An investment in a joint venture that is classified as held for sale under IFRS 5 *Non-current Assets Held for Sale and Discontinued Operations*, is accounted for under IFRS 5 and effectively scoped out of IFRS 11 and IAS 28.

3. Joint arrangements

IFRS 11 defines a joint arrangement as any arrangement where two or more parties have joint control. Some agreements may be referred to as joint arrangements, but are actually arrangements whereby one party has control of an entity. In these arrangements, the entity with control would consolidate it and the other parties would account for their interest in that entity based on the nature of their investment. Other arrangements may not be referred to as joint arrangements, but may qualify as joint arrangements, as defined by IFRS 11. In other words, the name of the agreement is not important – it only matters whether it meets the definition of a joint arrangement, as established by IFRS 11.

Excerpts from IFRS 11

- 4 A joint arrangement is an arrangement of which two or more parties have joint control.
- 5 A joint arrangement has the following characteristics:
 - (a) The parties are bound by a contractual arrangement.
 - (b) The contractual arrangement gives two or more of those parties joint control of the arrangement.

IFRS 11 notes that a contractual arrangement is often, but not always, in writing (although unwritten agreements are rare in practice). Statutory mechanisms can create enforceable arrangements, either on their own or in conjunction with contracts among the parties. A contractual agreement may be incorporated in the articles, charter or by-laws of the entity (or the separate vehicle, which is discussed in Section 5.1).

Contractual arrangements generally specify the following:

- ▶ Purpose, activity and duration of the joint arrangement
- ▶ Appointment of members of the board of directors (or equivalent governing body)
- ▶ Decision-making processes:
 - ▶ Matters requiring decisions from the parties
 - ▶ Voting rights of the parties
 - ▶ Required level of agreement for those matters
- ▶ Capital or other contribution requirements
- ▶ Sharing of assets, liabilities, revenues, expenses or profit or loss relating to the joint arrangement

Understanding the terms of the contractual arrangement is imperative for evaluating whether joint control exists, and if so, as discussed in Section 5, the type of joint arrangement.

3.1 Unit of account

IFRS 11 does not explicitly specify the unit of account for determining whether a joint arrangement exists. However, it seems that the IASB intended for the unit of account for a joint arrangement to be the activity that two or more parties have agreed to control jointly.

Excerpts from IFRS 11

BC35 Many respondents to ED 9 were concerned that joint ventures could be merely 'residuals'. This is because these respondents interpreted joint ventures to mean that after parties had identified rights to individual assets or obligations for expenses or financing, joint ventures would be merely any remaining assets and liabilities of the arrangement. As a result of these concerns, the Board clarified that the unit of account of a joint arrangement is the activity that two or more parties have agreed to control jointly, and that a party should assess its rights to the assets, and obligations for the liabilities, relating to that activity. Consequently, the term 'joint venture' refers to a jointly controlled activity in which the parties have an investment.

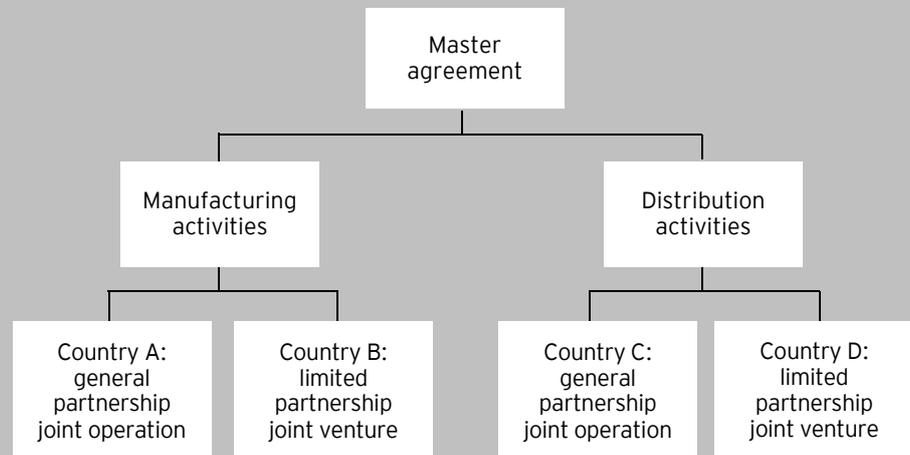
Therefore, it would seem that a party assesses its rights to the assets, and obligations for the liabilities, relating to that activity. When applied in practice, this raises the following questions:

- ▶ Can the unit of account be larger than an entity or separate vehicle? – Yes, if the activity that two or more parties have agreed to control jointly is larger than an entity or separate vehicle. This might be the case when there are multiple arrangements related to the same activity (we refer to these as layered agreements, which are discussed in Example 13 in Section 4).
- ▶ Can there be more than one unit of account within an entity or separate vehicle? – Yes, if there is more than one activity that two or more parties have agreed to control jointly within an entity or separate vehicle. Typically, we expect some sort of division or segmentation between the two activities within the entity or separate vehicle.
- ▶ Can there be more than one unit of account within a master agreement? – Yes, if there is more than one activity that two or more parties have agreed to control jointly within the master agreement. This is discussed in more detail in Example 1.

When identifying the unit of account for a joint arrangement, generally, it is appropriate to start by examining the contractual agreement. Frequently, each contractual agreement creates a single joint arrangement. However, some contracts may contain more than one joint arrangement. For example, a master agreement (referred to in IFRS 11 as a framework agreement) may contain the terms and conditions for numerous separate joint arrangements. Example 1 below illustrates a case where a master agreement may be accounted for as several distinct joint arrangements, each of which is classified as either a joint operation or a joint venture.

Example 1 – Master agreement for manufacturing and distribution

A single contract between two parties specifies the terms and conditions related to manufacturing and distribution activities, and dictates how these activities will be carried out in various jurisdictions through several entities.



The parties may determine that this agreement contains several discrete joint arrangements (one for each activity in each jurisdiction, which corresponds to a separate entity). In this case, each entity would likely be classified as a joint venture OR a joint operation. This would be the case if the terms and conditions relating to each activity were distinct for each entity.

Variation – A contract between two parties specifies the terms and conditions related to manufacturing and distribution activities, and dictates how these activities will be carried out in various jurisdictions. However, one party has the ability to direct the relevant activities in certain entities (e.g., the entity in Country A), and the other party has the ability to direct the relevant activities for others (e.g., the entity in Country B). In this case, there would not be joint control between the two parties because the decisions about the relevant activities do not require the unanimous consent of both parties. Rather, each party controls its respective entities.

In some cases, there will be multiple contractual agreements between parties related to the same activities, which may need to be analysed together to determine whether a joint arrangement exists, and if so, the type of joint arrangement (see Section 5).

In other cases, there may be a single master agreement between two parties that covers several different activities. Some of these activities may be controlled solely by one of the two parties, while other activities may be jointly controlled by the parties. Careful attention is required to determine the unit of account, and which arrangements, if any, are jointly controlled. Example 2 illustrates a case where a contract contains multiple agreements, only one of which is a joint arrangement.

Example 2 – Agreements with control and joint control

A and B enter into a contractual arrangement to buy a building that has 12 floors, which they will lease to other parties. A and B each are responsible for leasing five floors each, and each can make all decisions related to their respective floors and keep all of the income with respect to their floors. The remaining two floors will be jointly managed – all decisions with respect to those two floors must be unanimously agreed between A and B, and they will share all profits equally.

In this example, there are three arrangements:

- ▶ Two floors that A and B jointly control – a joint arrangement (within the scope of IFRS 11)
- ▶ Five floors that A controls – accounted for under other IFRS
- ▶ Five floors that B controls – accounted for under other IFRS

The unit of account as determined for A and B under IFRS 11 may differ from the unit of account for the previous owner under IAS 40 *Investment Property*.

4. Joint control

The crucial element of having a joint arrangement is joint control, and, therefore, it is important to understand its definition.

Excerpts from IFRS 11

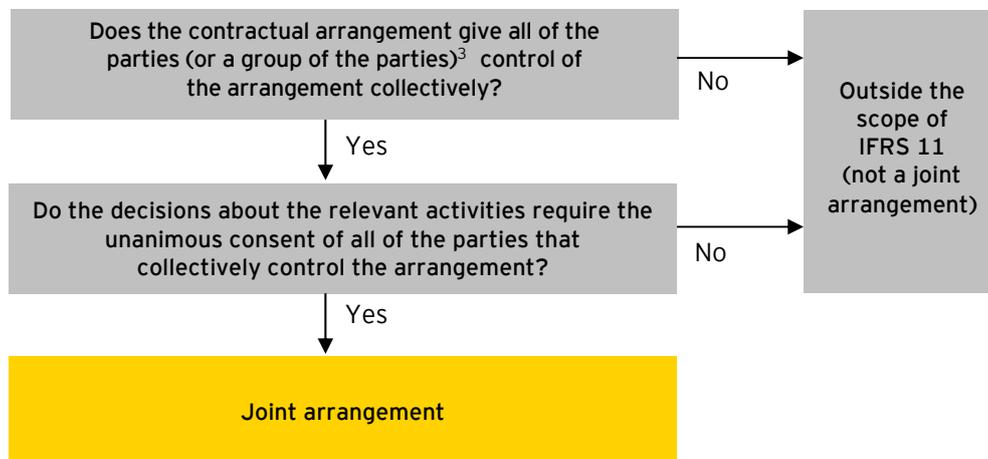
7 Joint control is the contractually agreed sharing of control of an arrangement, which exists only when decisions about the relevant activities require the unanimous consent of the parties sharing control.

The key aspects of joint control are as follows:

- ▶ Contractually agreed – See Section 3
- ▶ Control and relevant activities – IFRS 10 describes how to assess whether a party has control, and how to identify the relevant activities, which are described in more detail in our publication, *Applying IFRS - Challenges in adopting and applying IFRS 10*.¹ We discuss certain aspects of the concept of relevant activities and control that are most important to identifying joint control in Sections 4.1 and 4.2, respectively, of this publication
- ▶ Unanimous consent – IFRS 11 notes that unanimous consent means that any party (with joint control) can prevent any of the other parties, or a group of the parties, from making unilateral decisions about the relevant activities without its consent

The flow chart in Diagram 2 illustrates how to evaluate whether joint control exists²

Diagram 2 – Is it a joint arrangement?



¹ Available at ey.com/ifrs

² Diagram courtesy of IASB, IFRS 11 (paragraph B10).

³ The reference to 'a group of the parties' refers to a situation in which there is joint control between two or more parties, but other parties to the joint arrangement are passive investors (i.e., there are other parties in the arrangement who do not have joint control). While such investors are technically within the scope of IFRS 11, they account for their investment in accordance with the relevant standard (e.g., IAS 28 if they have significant influence, or as a financial instrument).

4.1 Relevant activities in a joint arrangement

To determine whether a contractual arrangement gives parties control of an arrangement collectively, it is necessary first to identify the relevant activities of that arrangement. That is, what are the activities that significantly affect the returns of the arrangement?

When identifying the relevant activities, consideration should be given to the purpose and design of the arrangement. In particular, consideration should be given to the risks to which the joint arrangement was designed to be exposed, the risks the joint arrangement was designed to pass on to the parties involved with the joint arrangement, and whether the parties are exposed to some or all of those risks.

In many cases, directing the strategic operating and financial policies of the arrangement will be the activity that most significantly affects returns. Often, the arrangement requires the parties to agree on both of these policies. However, in some cases, unanimous consent may be required to direct the operating policies, but not the financial policies (or vice versa). In such cases, since the activities are directed by different parties, the parties would need to assess which of those two activities (operating or financing) most significantly affects returns, and whether there is joint control over that activity.

4.1.1 Sequential activities

An arrangement may have different activities that occur at different stages. Generally, there are two situations:

- ▶ Parties may have rights to direct different activities
- ▶ Parties may collectively direct all of the activities

In the first situation, each party would assess whether it has rights to direct the activities that most significantly affect returns, and therefore whether it controls the arrangement. This situation does not result in joint control, and is described in Example 3, which is taken from IFRS 10, Example 1.

In Example 3, there is no joint control, because the parties do not collectively direct the activities of the arrangement. Rather, one party directs each activity. However, if the fact pattern were changed such that they collectively directed the activities of the arrangement, then there would be joint control. This is described in Example 4.

Example 3 – From IFRS 10 Example 1 - Directing sequential activities separately

Two investors form an investee to develop and market a medical product. One investor is responsible for developing and obtaining regulatory approval for the medical product. This includes having the unilateral ability to make all decisions relating to the development of the product and to obtain regulatory approval. Once the regulator has approved the product, the other investor will manufacture and market it – this investor has the unilateral ability to make all decisions about the manufacturing and marketing of the project. If all of the activities – developing and obtaining regulatory approval as well as manufacturing and marketing of the medical product – are relevant activities, each investor needs to determine whether it is able to direct the activities that most significantly affect the investee's returns.

Accordingly, each investor needs to consider whether developing and obtaining regulatory approval or the manufacturing and marketing of the medical product is the activity that most significantly affects the investee's returns and whether it is able to direct that activity. In determining which investor has power, the investors would consider:

- a) The purpose and design of the investee
- b) The factors that determine the profit margin, revenue and value of the investee as well as the value of the medical product
- c) The effect on the investee's returns resulting from each investor's decision-making authority with respect to the factors in (b)
- d) The investors' exposure to variability of returns

In this particular example, the investors would also consider:

- e) The uncertainty of obtaining regulatory approval and effort required to do so (considering the investor's record of successfully developing and obtaining regulatory approval of medical products)
- f) Which investor controls the medical product once the development phase is successful

Example 4 – Directing sequential activities jointly

Two investors form an investee to develop and market a medical product; this will occur in two phases. The first phase is developing the medical product and obtaining regulatory approval for that medical product. The second phase is the manufacturing and marketing of the medical product. The two investors agree that they will jointly make decisions over both phases.

Because the two investors make all decisions together throughout the term of the arrangement, it is not necessary to determine which of the above activities most significantly affects the returns of the arrangement, because they are all directed in the same manner. Therefore, the investors have joint control over the arrangement.

4.2 Rights to control collectively

To determine whether a contractual arrangement gives parties collective control of the arrangement, after identifying the relevant activities of that arrangement, it is necessary to determine what rights give a party the ability to direct the relevant activities. This is because, to have joint control, the parties must have collective control. To have control, the parties must collectively have power over the relevant activities.

In many cases, the relevant activities are directed by voting rights that are held in proportion to ownership interests. However, this is not always the case, and attention should be paid to the facts and circumstances in each case.

4.2.1 Protective rights

Protective rights are defined in IFRS 10.

Excerpt from Appendix A to IFRS 10

[Protective rights are] rights designed to protect the interest of the party holding those rights without giving that party power over the entity to which those rights relate.

Protective rights relate to fundamental changes to the activities of the arrangement, or apply in exceptional circumstances. Since power is an essential element of control, protective rights do not give a party control over the arrangement. Holding protective rights cannot prevent another party from having power over an arrangement. Protective rights are discussed in more detail in our publication *Applying IFRS 10*, Section 4.2.2. Accordingly, when assessing whether a group of the parties collectively control an arrangement (and therefore whether there is joint control), consideration must be given to whether rights held by any of the parties are:

- ▶ Protective (in which case, the other parties might collectively control the arrangement)
- ▶ Substantive (in which case, such rights could prevent the other parties from having joint control, or possibly give the holder of those rights control)

Example 5 illustrates this point with veto rights, which are frequently used to convey a protective right, although not all veto rights are protective rights.

Example 5 – Protective rights and joint control

A, B and C enter into a joint arrangement to conduct an activity in entity Z. The contractual agreement between A and B states that they must agree to direct all of the activities of Z. The agreement of C is not required, except that C has the right to veto the issuance of debt or equity instruments by Z. Issuing equity and debt instruments is deemed a protective right, because they represent fundamental changes in Z's business.

In this fact pattern, A and B have joint control over Z, because they collectively have the ability to direct Z, and the contractual agreement requires their consent. Although C is a party to the joint arrangement, C does not have joint control, because C only holds a protective right with respect to Z.

Rather than structuring the arrangement so that some parties hold a protective right, it may be structured so that, generally, all parties have a vote, but in the case of a tie, or disagreement, one party has the deciding vote. This is addressed in Section 4.3.2.

4.2.2 Potential voting rights and joint control

IFRS 11 does not explicitly address how potential voting rights are treated when assessing whether there is joint control. However, since the definition of joint control in IFRS 11 is based on the definition of control in IFRS 10, the requirements of IFRS 10 must be considered, if potential voting rights exist.

How we see it

Understanding the purpose and design of the potential voting right, including the context in which it was issued or granted, is important when evaluating whether the potential voting right is substantive and, if so, whether joint control exists. Our publication, *Applying IFRS 10*, Section 4.3.4, provides more information on how to assess if a potential voting right is substantive.

If the potential voting right is substantive, then the holder could have joint control together with the other parties, if the terms of the contractual arrangement confer joint control. For this to be the case, the holder and the other parties to the arrangement need to: (1) collectively control the arrangement; and (2) unanimously agree to direct the relevant activities of the arrangement.

4.2.3 Other evidence of joint control

As discussed in our publication, *Applying IFRS 10*, Section 4.5, in some cases, it may be difficult to determine whether a party's rights give it power over an arrangement. In such cases, the party considers other evidence that it has the current ability to direct the relevant activities. This evidence is also considered when evaluating if the parties to an arrangement control that arrangement collectively (i.e., in the evaluation of joint control).

How we see it

In addition to the examples of evidence listed in IFRS 10, another fact that may indicate that a party has control (or joint control), is whether the parties can obtain the financial information needed to account for the arrangement (e.g., to apply the equity method) and to provide the required disclosures. If a party cannot obtain information regarding an arrangement (e.g., because management of that arrangement refuses to provide it), this might indicate that the parties do not have collective control (and therefore, no joint control) over that arrangement.

4.2.4 Delegated decision-making

In some cases, one party may be appointed as manager of the arrangement. For example, this commonly occurs in the extractive and real estate industries. The manager is frequently referred to as the operator, but as IFRS 11 uses the terms joint operation and joint operator with specific meaning, to avoid confusion we refer to such parties as the manager. The other parties to the arrangement may delegate some of the decision-making rights to this manager.

Under IFRS 11, consideration is given to whether the manager controls the arrangement. When decision-making rights have been delegated, IFRS 10 describes how to assess whether the decision-maker is acting as a principal or an agent, and therefore, which party (if any) has control. Careful consideration of the following will be required:

- ▶ Scope of the manager's decision-making authority
- ▶ Rights held by others (e.g., protective, removal rights)
- ▶ Exposure to variability in returns through the remuneration of the manager

- ▶ Variable returns held through other interests (e.g., direct investments by the manager in the joint arrangement)

Each of the above is discussed in our publication *Applying IFRS 10*, Section 6 in more detail.

4.2.5 Related parties and de facto agents

IFRS 10 notes that, in some cases, one party may act as a *de facto* agent for another party (see our publication *Applying IFRS 10*, Chapter 7). *De facto* agents may include related parties (as defined in IAS 24 *Related Party Disclosures*).

Since the concepts of IFRS 10 extend to IFRS 11, consideration must be given to whether control or joint control exists, when one party is a *de facto* agent of another, as illustrated in Example 6.

Example 6 – De facto agents in joint control

A contractual arrangement has three parties: A has 50% of the voting rights and B and C each have 25%. The contractual arrangement between A, B and C specifies that at least 75% of the voting rights are required to make decisions about the relevant activities of the arrangement.

Analysis – There is neither control nor joint control, because more than one combination of parties can reach 75% and therefore direct the relevant activities.

Variation – If the facts and circumstances changed, such that C was deemed to be a *de facto* agent of B, then A and B would have joint control, because effectively B would direct 50% (in combination with C's 25%) and A would need B to agree to direct the relevant activities.

How we see it

Identifying *de facto* agents can be complex and requires judgement. Determining whether one party is a *de facto* agent of the other requires careful evaluation of the facts and circumstances.

4.2.6 Role of government

In some economies, the government may retain an interest in certain arrangements. When a government is a party to an arrangement, the arrangement needs to be carefully evaluated to determine whether joint control or control exists. For example, the government may own land, which is believed to contain oil reserves. If the government enters into a contractual arrangement with an oil company to drill for oil and sell the product, the oil company will have to evaluate the contractual terms of the arrangement closely to determine whether it has joint control, control, or some other type of interest. The ownership percentages in any separate vehicle do not necessarily determine whether there is control by one party or joint control. In some cases, the contractual terms may give all final decision-making authority over the development activities to the government, in which case, the government would have control. However, in other cases, the decision-making authority may require unanimous consent by the government and the oil company to direct the activities, in which case, they would have joint control.

4.3 Unanimous consent

IFRS 11 states that decisions about the relevant activities require the unanimous consent of all the parties, or a group of the parties, that collectively control the arrangement. Accordingly, it is not necessary for every party to the arrangement to agree to have unanimous consent. To have unanimous consent, only those parties that collectively control the arrangement must agree.

The requirement to have unanimous consent ensures that no single party controls the arrangement. IFRS 11 clarifies when unanimous consent exists, for example, in some cases, a contractual arrangement may require a minimum proportion of the voting rights to make decisions. When that minimum can be achieved by more than one combination of the parties agreeing, the arrangement is not a joint arrangement unless it specifies which parties (or combination of parties) are required to agree unanimously to decisions about the relevant activities of the arrangement. IFRS 11 provides some examples to illustrate this point, which are summarised in Diagram 3.

Diagram 3 – Joint control

	Scenario 1	Scenario 2
Requirement	75% vote to direct relevant activities	75% vote to direct relevant activities
Party A	50%	50%
Party B	30%	25%
Party C	20%	25%
Conclusion	Joint control – A and B collectively control the arrangement (since their votes, and only their votes, together meet the requirement). Because they are the only combination of parties that collectively control the arrangement, it is clear that A and B must unanimously agree.	No joint control – multiple combinations of parties could collectively control the arrangement (i.e., A and B or A and C could vote together to meet the requirement). Since there are multiple combinations, and the contractual agreement does not specify which parties must agree, there is no unanimous consent.

4.3.1 Passive investors

It is possible for two parties to an arrangement to have joint control, even if a third party has an interest in that joint arrangement, but does not have joint control. This situation is illustrated in Scenario 1 in Diagram 3 above.

IFRS 11 specifies the accounting for parties that participate in a joint arrangement, but who do not have joint control of that joint arrangement. This is discussed in Sections 6.3 and 7.1 for joint operations and joint ventures, respectively.

4.3.2 Ultimate voting authority

Sometimes an arrangement is structured so that all parties have a vote, but in the case of a tie (deadlock), or disagreement, one party has the deciding vote. If any single party could direct the relevant activities unilaterally, there would not be joint control. Examples 7 and 8 illustrate this point.

Example 7 – Ultimate decision-making authority – no joint control No. 1

G and H enter into an agreement and set up a joint steering committee. One party has ultimate decision-making authority in cases where the joint steering committee cannot reach an agreement. In this case, there would not be joint control, since the agreement of the other party is not needed.

To evaluate whether the party with the deciding vote has control, one would also need to assess whether it has exposure to variable returns, and the ability to affect those returns through its power, as required by IFRS 10.

Just because one party has a deciding vote does not necessarily mean that it has control, particularly if other parties can act without the agreement of that party. This is illustrated in Example 8.

Example 8 – Ultimate decision-making authority – no joint control No. 2

I, J and K enter into an agreement and set up a joint steering committee. Each party has one vote and two votes are needed to carry a motion. K has ultimate decision-making authority in cases where the joint steering committee cannot reach an agreement. For example, if no combination of I, J and K can agree with each other, K would have the ultimate decision-making authority.

There is not joint control, since I and J could agree together, without the agreement of K.

4.3.3 Arbitration

Contractual arrangements often include terms and conditions relating to the resolution of disputes, and may also provide for arbitration. The existence of such terms and conditions does not prevent the arrangement from being jointly controlled and, consequently, from being a joint arrangement.

4.3.4 Implicit joint control

Joint control need not be explicitly stated in the terms of the contractual arrangement to exist. That is, joint control can exist implicitly, depending on the contractual terms of the arrangement, and whether the terms of the arrangement explicitly, or implicitly, require unanimous consent of the parties.

For example, if two parties have equal (50%) ownership of a separate vehicle, joint control could exist even if the terms of the contractual arrangement do not specify unanimous consent over the relevant activities. The following excerpt from IFRS 11 illustrates this concept.

Excerpt from IFRS 11

B7 Sometimes the decision-making process that is agreed upon by the parties in their contractual arrangement implicitly leads to joint control. For example, assume two parties establish an arrangement in which each has 50 per cent of the voting rights and the contractual arrangement between them specifies that at least 51 per cent of the voting rights are required to make decisions about the relevant activities. In this case, the parties have implicitly agreed that they have joint control of the arrangement because decisions about the relevant activities cannot be made without both parties agreeing.

In the fact pattern above, it is implicit in the arrangement that the two parties must agree. This is because in order for there to be majority agreement, both parties would need to agree, since they each have 50%. This example from IFRS 11 illustrates that it is possible to have implicit unanimous consent to have joint control.

Determining whether joint control exists implicitly depends on a careful evaluation of the contractual terms of the arrangement. It is possible that two parties have equal ownership interests, but the relevant activities are directed by one party according to the contractual arrangement between them. In this case, the party that has the contractual right to direct the relevant activities would have control (i.e., joint control would not exist). See our publication, *Applying IFRS 10*, Section 4.4 for more information.

As discussed in Section 3, IFRS 11 notes that statutory mechanisms can create enforceable arrangements. Furthermore, the articles, charter or by-laws of the separate vehicle (when one exists) are also part of the contractual agreement between parties. Accordingly, when evaluating whether an arrangement implicitly results in joint control, consideration needs to be given to the statutory requirements in the relevant jurisdiction under which the arrangement was established, as that might affect the conclusion.

4.4 Other practical issues with assessing joint control

4.4.1 Lease vs a joint arrangement

In some cases, careful consideration will need to be given to the terms and conditions of an arrangement to determine whether a party is leasing an asset that is controlled by another party (and may with other parties, effectively lease the asset for its entire life), or whether the parties have a joint arrangement. These two cases are illustrated in Example 9.

Example 9 – A lease or a joint arrangement?

Five parties jointly buy an aircraft. By contractual agreement, each party has the right to use the aircraft for a certain number of days each year and shares proportionately in the maintenance costs. They share decision-making regarding the usage, maintenance and disposal of the aircraft, which are the relevant activities for the aircraft. Those decisions require the unanimous agreement of all of the parties. The contractual agreement covers the expected life of the aircraft and can be changed only by unanimous agreement.

Analysis – The agreement is a joint arrangement. Through the contractual agreement, the five parties agreed to share the use and costs of maintaining the aircraft, and decisions require unanimous consent.

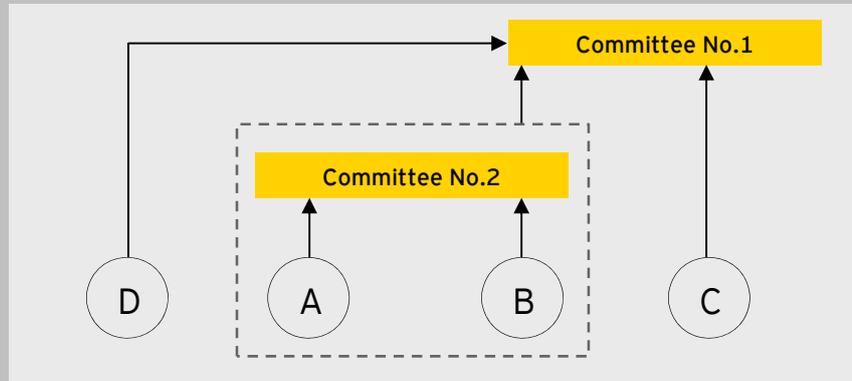
Variation – If, instead, the five parties entered into an agreement with a separate vehicle that controlled the aircraft this may be a lease. This would be the case if they did not have the ability to direct the relevant activities (for example, if the management of the separate vehicle made decisions regarding maintenance or disposal).

4.4.2 Evaluate multiple agreements together

Although not explicitly required by IFRS 11, in some cases, it may be necessary to evaluate multiple agreements together, to understand the purpose and design of an arrangement and to determine if there is joint control. A party may appear to have joint control of a joint arrangement when considering an agreement in isolation, but that party may not have joint control when considered in the full context of its purpose and design. Example 10 illustrates this point.

Example 10 – Layered agreements

A, B, C and D enter into agreement No. 1 to undertake oil and gas exploration. Committee No. 1 is formed to direct all activities related to the activity including review and approval of annual budgets and operating policies. Committee No. 1 consists of four members nominated by A, B, C and D. The decisions of Committee No. 1 require the unanimous vote of the members.



A and B enter into agreement No. 2, which establishes Committee No. 2 to coordinate cooperation between A and B, with respect to the same oil and gas exploration activity. A and B each appoint one representative to Committee No. 2. Committee No. 2 has the power to make decisions to be submitted for approval to Committee No. 1. Any matter to be decided by Committee No. 2 requires the consent of both parties. However, if agreement cannot be reached between A and B, B has the deciding vote. The decisions made in Committee No. 2 are binding on A and B and they must vote accordingly in Committee No. 1.

In this fact pattern, there are two separate contractual agreements. However, they are evaluated together to determine if there is a joint arrangement, because they relate to the same oil and gas exploration activity. For example, if agreement No. 1 were considered in isolation, it would appear that A, B, C and D all have joint control over the arrangement.

However, agreement No. 1 should be evaluated together with agreement No. 2. Accordingly, only B, C, and D would have joint control over the joint arrangement. Since B can effectively direct A how to vote (by virtue of agreement No. 2) in Committee No. 2, A does not have joint control with the other parties, since it is effectively a *de facto* agent of B.

5. Classification of a joint arrangement

A joint arrangement is classified as either a joint operation or a joint venture, as shown in Diagram 4.

Diagram 4 – Joint operation vs joint venture

Type of Arrangement	Joint operation	Joint venture
Definition	The parties with joint control have rights to the assets and obligations for the liabilities of the arrangement.	The parties with joint control have rights to the net assets of the arrangement.
Parties with joint control	Joint operator – a party with joint control in a joint operation	Joint venturer – a party with joint control in a joint venture
Accounting overview	<p>A joint operator accounts for the following in accordance with the applicable IFRS:</p> <ul style="list-style-type: none"> ▶ Its assets, including its share of any assets held jointly ▶ Its liabilities, including its share of any liabilities incurred jointly ▶ Its revenue from the sale of its share of the output arising from the joint operation ▶ Its share of revenue from the sale of the output by the joint operation ▶ Its expenses, including its share of any expenses incurred jointly 	A joint venturer accounts for its investment in the joint venture using the equity method.

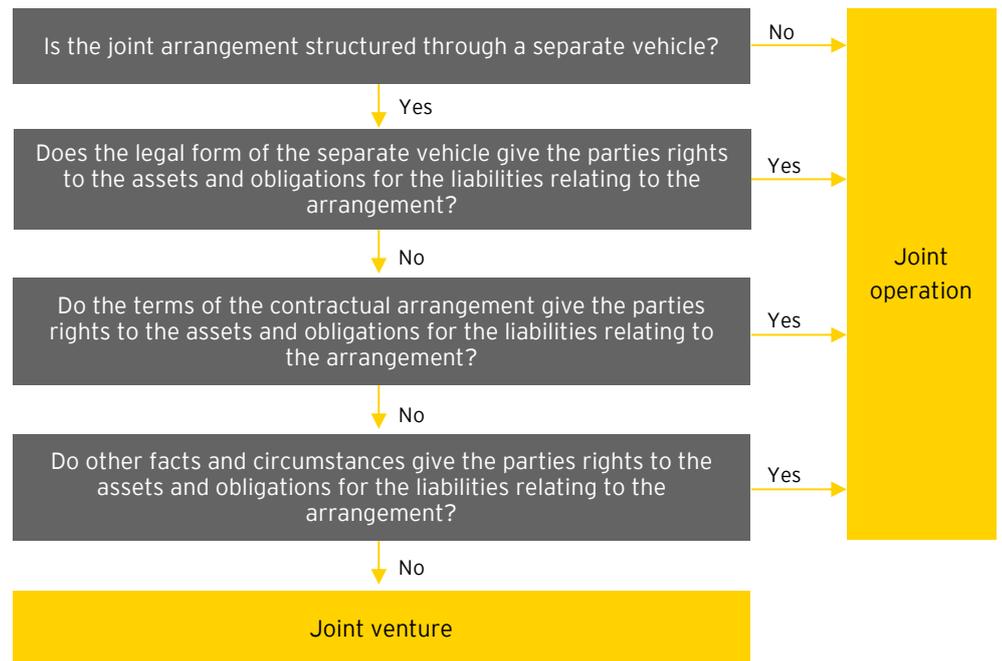
Although the terms joint venture and joint operation are broadly used in practice, they are specifically defined in IFRS 11.

When classifying a joint arrangement as either a joint operation or a joint venture, the first step is to assess whether there is a separate vehicle. If not, the joint arrangement is automatically a joint operation. However, if there is a separate vehicle, the following factors need to be considered:

- ▶ Legal form of the separate vehicle
- ▶ Contractual terms and conditions
- ▶ Other facts and circumstances

This process is illustrated in Diagram 5 (based on IFRS 11.B33) and each of these is discussed in more detail below. The flow chart illustrates several criteria that need to be met for the joint arrangement to be classified as a joint venture. If just one of the criteria indicates that the parties have the rights to the assets and obligations for the liabilities, the joint arrangement would be classified as a joint operation. IFRS 11 also includes examples illustrating this evaluation.

Diagram 5 – Classifying a joint arrangement



When classifying a joint arrangement, the IASB generally expects that all parties to the joint arrangement would reach the same conclusion regarding classification. To reach different conclusions regarding the classification of a joint arrangement would mean that the parties have different rights to assets and obligations for the liabilities within the same separate vehicle, which the IASB believes would be rare.

It may be necessary to analyse two (or more) agreements together, such as when there is a master agreement (see Section 3.1). IFRS 11 also states that the classification of a joint arrangement should also be made in the context of the normal course of business.

Excerpt from IFRS 11

B14 The classification of joint arrangements required by this IFRS depends upon the parties' rights and obligations arising from the arrangement in the normal course of business.

These concepts are discussed in more detail in the context of analysing the contractual terms of the arrangement, and the other facts and circumstances in Sections 5.3 and 5.4, respectively.

How we see it

The requirement to classify a joint arrangement based on the normal course of business is consistent with the requirement to consider the purpose and design of an investee in IFRS 10 (see our publication, *Applying IFRS 10*, Section 1, for additional discussion on this point). We believe that the purpose and design of a joint arrangement is an important consideration in determining the appropriate classification.

5.1 Separate vehicle

The first factor in classifying a joint arrangement is the assessment of whether a separate vehicle exists. If yes, then further evaluation must be completed to classify the joint arrangement. However, if no separate vehicle exists, then the joint arrangement is always a joint operation.

Excerpt from IFRS 11

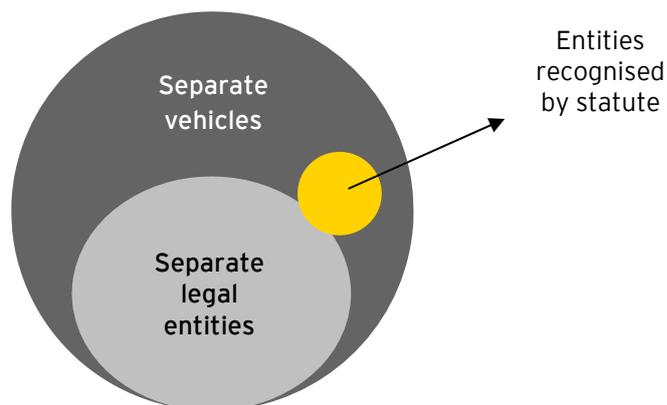
Separate vehicle: A separately identifiable financial structure, including separate legal entities or entities recognised by statute, regardless of whether those entities have a legal personality.

For example, a partnership, or corporation would be considered a separate vehicle. In some cases, a trust or a syndicate may also be considered a separate vehicle. Consideration should be given to local laws. In some jurisdictions, an oral agreement is considered sufficient to create a contractual partnership, and thus, the hurdle for having a separate vehicle could be quite low.

A contract may create a separate vehicle, such as when it creates a deemed separate entity (referred to as a silo in IFRS 10). A silo exists when specified assets of an arrangement are the only source of payment for specified liabilities of an arrangement, and parties other than those with the specified liability do not have rights or obligations related to the specified assets or to residual cash flows from those assets. That is, a silo exists when, in substance, all the assets, liabilities and equity of that deemed separate entity are ring-fenced from the host arrangement. See our publication, *Applying IFRS 10*, Section 8.1, for more information on identifying silos.

The term 'separate vehicle' is broader than 'entity' (see Diagram 6). In some jurisdictions, separate vehicles may be created to establish a joint arrangement, but the separate vehicles do not meet the definition of an entity in that jurisdiction. These arrangements will need further evaluation for classification as either a joint operation or a joint venture.

Diagram 6 – Legal entities are a subset of separate vehicles



The reason for determining whether there is a separate vehicle is that the IASB believes it would be rare that a joint arrangement would give the parties rights to the net assets without having a separate vehicle. Thus, if no separate vehicle exists, the process is cut short to conclude that the joint arrangement is a joint operation, as shown in Diagram 5.

5.2 Legal form of the separate vehicle

Once it is determined that a separate vehicle exists, the second step is to analyse the legal form of the separate vehicle to determine whether it gives the parties rights to net assets, or rights to the assets and obligations for the liabilities of the arrangement, i.e., does the separate vehicle confer separation between the parties and the separate vehicle?

The impact of local laws should be carefully assessed when analysing the form of the separate vehicle. For example, in many countries, a corporation confers separation between the parties and the separate vehicle and also provides the parties with rights to net assets (which are indicators of being a joint venture). That is, the liabilities of the corporation are limited to the corporation. Creditors do not have recourse to the investors in the corporation for those liabilities. However, this may not be true in all countries.

Similarly, partnerships that have unlimited liability (which are common in many countries) often do not confer separation between the parties and the separate vehicle. That is, they provide the partners with rights to the assets and obligations for the liabilities, indicating that the arrangement is a joint operation. When creditors of the partnership have direct recourse to the joint arrangement partners, the partners are the primary obligor, which is indicative of a joint operation. However, in a partnership where creditors only have recourse to the partners after the partnership has defaulted, there is separation between the partners and the vehicle. The liability of the partners as secondary obligor is akin to a guarantee. This would be an indicator of a joint venture.

5.3 Contractual terms

The next step in classifying a joint arrangement is to examine the contractual terms of the arrangement, to determine whether they provide the parties with rights to the net assets (a joint venture) or rights to the assets and obligations for the liabilities (a joint operation). This is because even if the legal form of the separate vehicle establishes rights for each of the parties, the contractual terms of the joint

arrangement may unwind the effects of the legal form and give the parties rights to the assets, and obligations for the liabilities.

IFRS 11 includes examples of common contractual terms found in joint arrangements, and indicates whether these are examples of joint operations or joint ventures. These are summarised in Diagram 7.

IFRS 11 also includes an example of how the contractual terms of the joint arrangement can modify the form of the separate vehicle. This is illustrated in Example 11.

Example 11 – Modification of legal form by contractual terms

A and B jointly establish a corporation (C) over which they have joint control. The fact that there is a separate vehicle, and the legal form of the separate vehicle (a corporation) indicates that C is a joint venture.

However, the contractual arrangement states that A and B have rights to the assets of C and are obligated for the liabilities of C in a specified proportion. Effectively, this contractual term unwinds the effects of the legal form (corporation). Therefore, C is a joint operation.

Diagram 7 – Examples of common contractual terms in a joint arrangement

	Joint operation	Joint venture
Rights to assets	The parties share all interests (e.g., rights, title or ownership) in the assets relating to the arrangement in a specified proportion.	The assets brought into the joint arrangement or subsequently acquired by it are the arrangement's assets. The parties have no interests (i.e., no rights, title or ownership) in the assets of the arrangement.
Obligations for liabilities	The parties share all liabilities, obligations, costs and expenses in a specified proportion.	The joint arrangement is liable for the debts and obligations of the arrangement.
	The parties are jointly and severally liable for the obligations of the arrangement.	The parties are liable under the arrangement only to the extent of their respective investments in the arrangement, or to their respective obligations to contribute any unpaid or additional capital to the arrangement, or both.
	The parties are liable for claims raised by third parties.	Creditors of the joint arrangement do not have rights of recourse against any party with respect to debts or obligations of the arrangement.

5.3.1 Guarantees

Parties to joint arrangements may provide guarantees to third parties. For example, a party to a joint arrangement may provide a guarantee or commitment that:

- ▶ Services provided by the joint arrangement to the third party will be of a certain quality or nature
- ▶ It will repay funding received from the third party
- ▶ It will support the joint arrangement in the event of distress

One might think that providing a guarantee (or commitment to provide a guarantee) gives a party an obligation for a liability, which would indicate that the joint arrangement should be classified as a joint operation. However, IFRS 11 states this is not the case.

How we see it

Although perhaps counter-intuitive, the fact that a guarantee is not determinative of the classification of a joint operation is consistent with the principles in IFRS 11. This is because the guarantee does not give the guarantor a present obligation for the underlying liabilities. Accordingly, a guarantee is not determinative of having an obligation for a liability.

If the issuer of the guarantee has to pay or perform under that guarantee, this may indicate that facts and circumstances have changed, or the trigger event may be accompanied by a change in the contractual terms of the arrangement. These changes would trigger a reassessment of whether the arrangement is still subject to joint control as discussed in Section 8, and if so, whether the joint arrangement is a joint operation or a joint venture. The party issuing the guarantee must still account for the guarantee in accordance with IAS 39 or IFRS 9.

5.3.2 Contractual terms upon liquidation or dissolution of joint arrangement

In some joint arrangements, the parties contribute assets to the joint arrangement to be used in the activity for as long as it continues to operate. However, if the joint arrangement is liquidated or dissolved, the contributed assets revert to the contributing party. The question is whether this contractual term gives the parties rights to the assets. If so, this would mean that the joint arrangement is classified as a joint operation.

How we see it

In our view, a contractual agreement whereby assets contributed to a joint arrangement revert back to the contributing party upon liquidation or dissolution of a joint venture, does not necessarily mean that the joint arrangement is a joint operation. This is because the contributing party does not expect to receive the contributed assets in the normal course of business.

All relevant facts and circumstances should be considered in reaching a conclusion. For example, if the party contributing the asset has a currently-exercisable call option on that asset, this fact should be considered in evaluating whether the party has rights to the assets and obligations for the liabilities of the joint arrangement; that is, whether it is a joint operation. The call option would also need to be accounted for in accordance with the relevant IFRS.

5.4 Other facts and circumstances

If the preliminary assessment of the legal form and the contractual terms of the joint arrangement indicate that a joint arrangement may be a joint venture, then the parties must consider any other facts and circumstances to determine whether they have rights to the assets and obligations for the liabilities, which would make it a joint operation.

The IFRS Interpretations Committee (IC) has received a number of requests regarding application of IFRS 11. At the meeting in January 2014, the IFRIC discussed whether the assessment of other facts and circumstances should be based only on contractual (and legal) enforceable terms. The staff analysis was split into five issues:

- ▶ A—Should the assessment of ‘other facts and circumstances’ be based only on contractual (and legal) enforceable terms?
- ▶ B—Does the fact that the output from the joint arrangement is sold at a market price prevent the joint arrangement from being classified as a joint operation, when assessing ‘other facts and circumstances’?
- ▶ C—Does financing from a third party prevent an arrangement from being classified as a joint operation?
- ▶ D—Does the nature of the output produced by the joint arrangement determine the classification of a joint arrangement when assessing ‘other facts and circumstances’?
- ▶ E—When assessing ‘other facts and circumstances’ in the case in which parties are taking substantially all of the output, is the assessment based on volumes or monetary values?

With regard to Issue A, the IC tentatively decided not to add the issue to its agenda, as paragraph 14 of IFRS 11 requires the classification of a joint arrangement as a joint operation or a joint venture to be based upon rights to the assets and obligations for the liabilities of the parties to the arrangement, and that rights and obligations, by nature, are enforceable. The IC also noted that paragraph B30 of IFRS 11 describes that when ‘other facts and circumstances’ give the parties rights to the assets and obligations for the liabilities relating to the arrangement, the assessment of ‘other facts and circumstances’ would lead to the joint arrangement being classified as a joint operation. Consequently, the assessment of other facts and circumstances should focus on whether they create enforceable rights to the assets and obligations for the liabilities.

With regard to the other issues, the IC noted that it is important to understand how and why particular facts and circumstances create rights and obligations that result in the joint arrangement being classified as a joint operation. The IC asked the staff to develop examples to analyse this matter. These examples should include fact patterns illustrating Issues B-E and consider the application of IFRS 11 to some common joint arrangement structures. The IC also requested that this analysis consider the implications for accounting within separate financial statements. Upon consideration of this further analysis, the IC will decide whether to recommend adding examples or other guidance to the standard.

When classifying a joint arrangement as either a joint operation or a joint venture, it is critical to understand the purpose and design of the joint arrangement. In addition, it is important to understand whether the joint arrangement:

- ▶ Primarily aims to provide the parties with an output (i.e., the parties have rights to substantially all of the economic benefits of the assets)
- ▶ Depends on the parties on a continuous basis for settling its liabilities

If both of the above are characteristics of the joint arrangement, then it is a joint operation. In some cases, judgement will be needed to assess whether these criteria are met. Diagram 8 illustrates how these factors might be present in a joint arrangement.

Diagram 8 – Other facts and circumstances

	Joint operation	Joint venture
Restrictions on selling output	Restricted from selling output to third parties	None; may be able to sell output to other parties
Requirements to purchase output	Parties (individually or collectively) must purchase substantially all of output produced	None; other parties might purchase output
Selling price of output to parties	At cost (or designed for joint arrangement to break even)	At market (or designed for joint arrangement to generate a profit)

Example 12 (summarised from IFRS 11) illustrates how the facts and circumstances might indicate that the joint arrangement is a joint operation, even if the legal form and contractual terms point towards the joint arrangement being a joint venture.

Example 12 – Modification of legal form by facts and circumstances

A and B jointly establish a corporation (C) over which they have joint control. The existence of a separate vehicle, which is in the legal form of a corporation, initially indicates that the assets and liabilities held in C are the assets and liabilities of C, and therefore that C is a joint venture. No contractual terms indicate that A and B have rights to the assets, or obligations for the liabilities, so the arrangement still appears to be a joint venture.

However, A and B agree to the following:

- ▶ A and B will purchase all the output produced by C in a ratio of 50:50.
- ▶ C cannot sell any of the output to third parties, unless A and B approve it. Because the purpose of the arrangement is to provide A and B with output they require, sales to third parties are not expected to occur.
- ▶ The price of the output sold to A and B is set by A and B at a level that is designed to cover the costs of production and administrative expenses incurred by C. The arrangement is intended to operate at a break-even level.

Analysis

- ▶ The obligation of A and B to purchase all of the output produced by C reflects the exclusive dependence of C upon A and B for the generation of cash flows and, thus, implicitly that A and B have an obligation for the liabilities of C.
- ▶ The fact that A and B have rights to all of the output produced by C means that A and B are consuming, and therefore have rights to, all of the economic benefits of the assets of C. These facts and circumstances indicate that the arrangement is a joint operation.

Variation 1 – If, instead of A and B using their share of the output themselves, they sold their share of the output to third parties, the joint arrangement would still be classified as a joint operation.

Variation 2 – If A and B changed the terms of the contractual arrangement so that the arrangement was able to sell output to third parties, this would result in C assuming demand, inventory and credit risks, such that A and B would not have substantially all of the economic benefits. Accordingly, in this case, the joint arrangement would likely be classified as a joint venture.

5.4.1 Output taken by only one party

The examples and analysis in IFRS 11 discuss joint arrangements in which the parties to the joint arrangement share in the output. However, in some cases, one party receives or purchases all of the output. For example, this may be the case when:

- ▶ One of the parties is not in a business that is aligned with the activity of the joint arrangement (e.g., a local government has joint control with a foreign entity). Generally, the party that does not receive output is compensated in some other manner, relative to its respective interests in the joint arrangement.
- ▶ The party that receives all of the output is acting as an agent for the other parties to the joint arrangement, and acting on the other party's behalf.

How we see it

In such cases, the first step should be to confirm that there actually is joint control. A reassessment of the facts and circumstances may indicate that the party that receives all of the output controls the arrangement.

However, if there is joint control, this would likely be a joint operation. This is because the parties collectively have rights to substantially all of the economic benefits of the assets of the joint arrangement. In our view, the nature of the assets is different for each party. That is, one party receives a tangible output, whereas the other receives a financial asset, but both parties have rights to the assets, and obligations for the liabilities of the joint arrangement, rather than rights to the net assets of the joint arrangement.

5.4.2 Assessing whether parties provide cash flows

As noted above, IFRS 11 states that if a joint arrangement depends on the parties on a continuous basis to settle its liabilities, this would be indicative of it being a joint operation.

Excerpt from IFRS 11

- B31 When the activities of an arrangement are primarily designed for the provision of output to the parties, this indicates that the parties have rights to substantially all the economic benefits of the assets of the arrangement. The parties to such arrangements often ensure their access to the outputs provided by the arrangement by preventing the arrangement from selling output to third parties.
- B32 The effect of an arrangement with such a design and purpose is that the liabilities incurred by the arrangement are, in substance, satisfied by the cash flows received from the parties through their purchases of the output. When the parties are substantially the only source of cash flows contributing to the continuity of the operations of the arrangement, this indicates that the parties have an obligation for the liabilities relating to the arrangement.

Questions have arisen as to whether parties would be considered 'substantially the only source of cash flows' if they provide cash flows at inception of a joint arrangement, but are not expected to thereafter, and no other parties are expected to provide cash flows until the end of an activity. Alternatively, parties might provide cash flows through a series of 'cash calls' throughout the arrangement.

How we see it

In our view, the provision of cash flows at the inception of a joint arrangement, and/or the expectation that no other parties will provide cash flows until the end of an activity, are not conclusive in determining whether there is an obligation for a liability. That is, it is not conclusive whether the joint arrangement is a joint operation or a joint venture. These situations are illustrated in Example 13.

Example 13 – Construction and real estate sales

Fact pattern – A separate vehicle is established, over which two parties have joint control. Neither the legal form nor the contractual terms of the joint arrangement give the parties rights to the assets or obligations for the liabilities of the arrangement. Other facts and circumstances are, as follows:

- ▶ The purpose of the joint arrangement is to construct a residential complex for selling residential units to the public
- ▶ Contributed equity by the parties is sufficient to purchase land and raise debt finance from third parties to fund construction
- ▶ Sales proceeds will be used as follows (in this priority):
 - ▶ Repayment of external debt
 - ▶ Remaining profit distributed to parties

Analysis – Since there is a separate vehicle, and because neither the legal form nor the contractual terms of the joint arrangement give the parties rights to the assets or obligations for the liabilities of the vehicle, the preliminary analysis indicates that this is a joint venture. The fact that the parties are the only source of cash flows at inception is not conclusive whether the facts and circumstances indicate that the parties have rights to the assets, or obligations for the liabilities. That is, more information is needed and judgement will be required in determining whether this is a joint venture or a joint operation.

Variation – The contributed equity is not sufficient to purchase the land and raise debt financing. There is an expectation, or requirement, that the parties will have to contribute cash to the joint arrangement through a series of cash calls. The fact that the parties are expected to be a source of cash flows is not sufficiently conclusive to indicate that the parties have rights to the assets, and/or obligations for the liabilities. That is, more information is needed before concluding if this is a joint venture or a joint operation.

6. Accounting for joint operations

For a joint operation, the joint operator recognises its:

- ▶ Assets, including its share of any assets held jointly
- ▶ Liabilities, including its share of any liabilities incurred jointly
- ▶ Revenue from the sale of its share of the output arising from the joint operation
- ▶ Share of the revenue from the sale of the output by the joint operation
- ▶ Expenses, including its share of any expenses incurred jointly

IFRS 11 requires each of these items to be accounted for in accordance with the IFRS applicable.

Careful consideration should be given to the nature of the rights to the assets, and the obligations for the liabilities (or the share of assets, liabilities, revenues, and expenses) if any, of the joint operation. That is, what does the joint arrangement actually entitle the joint operators to, and make them responsible for?

For example, one of the joint operators may have a direct legal liability for the entire balance of certain liabilities of the joint operation. It may also have a right to reimbursement by the other parties for their share of that liability of the joint operation. This situation frequently arises when the joint operator is the manager of the joint operation.

A joint operator who is responsible for the entire balance of the obligation would recognise 100% of that liability and would recognise a receivable for the reimbursement due from the other parties for their share of such liability. IFRS prohibits the offsetting of the liability against the receivable. But, other than the gross-up of the balance sheet, there would be no impact on the financial statements (e.g., profit) when the third party share of the liability and the receivable are for equal amounts. In most circumstances, this will be the case when the ability of the other parties to reimburse the joint operator for their share of the liabilities is not in doubt.

However, there may be instances in which the other parties are unable to pay. In these cases, the joint operator would not be able to recognise a receivable for the full amount due. Accordingly, since the receivable would be impaired (or less than the third party share of the liability recorded), this situation would impact a joint operator's financial statements (e.g., a reduction in profit).

In some cases, the joint arrangement (or legal form of the separate vehicle, if applicable) gives joint and several liability for the obligations of the arrangement. This may result in the joint operator recognising the entire obligation due, not just its share. The facts and circumstances need to be assessed in each case, and the liability accounted for in accordance with IAS 37 *Provisions, Contingent Liabilities and Contingent Assets*.

A party to the joint arrangement who has an obligation to reimburse another party would recognise a financial liability for the amount related to the reimbursement.

How we see it

It will be critical for joint operators to fully understand the rights and obligations in joint arrangements, and how they are shared amongst the parties.

When a joint operator is required to recognise 100% of a liability, because it is responsible for the entire balance of the obligation of the joint operation, its net financial position and profit will usually not be negatively affected. This is because the joint operator usually will also recognise a separate receivable from the other joint operators and such receivable is usually collectible. However, the joint operator should consider the impact on its key ratios, which may be affected by the gross-up in the balance sheet.

6.1 Difference from proportionate consolidation

An entity's rights and obligations for the assets, liabilities, revenues and expenses relating to a joint operation as specified in the contractual arrangement, are the basis for accounting for a joint operation under IFRS 11. This may differ from its ownership interest in the joint operation, which would have been the basis for proportionate consolidation under the previous standard, IAS 31.

When a joint operator has rights to a specified percentage of all assets and obligations for the same percentage of all liabilities, there would probably not be a difference between the accounting for a joint operation and proportionate consolidation in practice.

Excerpt from IFRS 11

BC38 The Board noted that there are two main differences between recognising assets, liabilities, revenues and expenses relating to the activity of the joint operation and proportionate consolidation. The first difference relates to the fact that the rights and obligations, as specified in the contractual arrangement, that an entity has with respect to the assets, liabilities, revenues and expenses relating to a joint operation might differ from its ownership interest in the joint operation. The IFRS requires an entity with an interest in a joint operation to recognise assets, liabilities, revenues and expenses according to the entity's shares in the assets, liabilities, revenues and expenses of the joint operation as determined and specified in the contractual arrangement, rather than basing the recognition of assets, liabilities, revenues and expenses on the ownership interest that the entity has in the joint operation. The second difference from proportionate consolidation is that the parties' interests in a joint operation are recognised in their separate financial statements. Consequently, there is no difference in what is recognised in the parties' separate financial statements and the parties' consolidated financial statements or the parties' financial statements in which investments are accounted for using the equity method.

However, when the joint operator has differing rights (and percentages) to various assets, and/or different obligations for various liabilities, the financial statements would likely change as a result of accounting for those individual rights and obligations, as compared with the result from proportionately consolidating a blended percentage of all assets and liabilities. Example 14 illustrates the accounting for a joint operation under IFRS 11.

Example 14 – Accounting for rights to assets and obligations for liabilities

D and E establish a joint arrangement (F) using a separate vehicle, but the legal form of the separate vehicle does not confer separation between the parties and the separate vehicle itself. That is, D and E have rights to the assets and obligations for the liabilities of F (F is a joint operation). Neither the contractual terms, nor the other facts and circumstances indicate otherwise. Accordingly, D and E account for their rights to assets and their obligations for liabilities relating to F in accordance with the relevant IFRS.

D and E each own 50% of the equity (e.g., shares) in F. However, the contractual terms of the joint arrangement state that D has the rights to all of Building No. 1 and the obligation to pay all the third party debt in F. D and E have rights to all other assets in F, and obligations for all other liabilities in F in proportion to their equity interests (i.e., 50%).

F's balance sheet is as follows (in CUs):

Assets		Liabilities and equity	
Cash	20	Debt	120
Building No. 1	120	Employee benefit plan obligation	50
Building No. 2	100	Equity	70
Total assets	240	Total liabilities and equity	240

Under IFRS 11, D would record the following in its financial statements, to account for its rights to the assets in F and its obligations for the liabilities in F. This likely will differ from the amounts recorded using proportionate consolidation.

Assets		Liabilities and equity	
Cash	10	Debt ⁽²⁾	120
Building No. 1 ⁽¹⁾	120	Employee benefit plan obligation	25
Building No. 2	50	Equity	35
Total assets	180	Total liabilities and equity	180

⁽¹⁾ Since D has the rights to all of Building No. 1, it records that amount in its entirety.

⁽²⁾ D's obligations are for the third-party debt in its entirety.

6.2 Determining the relevant IFRS

Joint operators are required to recognise their rights to assets and their obligations for liabilities in accordance with the relevant IFRS. In some cases, the relevant IFRS is clear, but questions have arisen in other cases.

Excerpt from IFRS 11

BC39 Many respondents to ED 9 were not clear whether parties to a joint operation that had rights to the assets should recognise a 'right to use' or a 'right to a share' or whether they should instead directly recognise 'their share of the joint assets, classified according to the nature of the asset'. The concern raised by this uncertainty was the different accounting implications of these interpretations – i.e., accounting for rights or accounting for shares of assets. The Board concluded that a party to a joint operation should recognise its assets or its share of any assets in accordance with the IFRSs applicable to the particular assets.

The illustrative examples of joint operations in IFRS 11 refer to recognising the joint operator's share of assets (e.g., property, plant and equipment, accounts receivable, cash, share of production), rather than recognising a 'right of use'.

How we see it

A joint operator will need to carefully analyse the nature of its rights to assets when determining the appropriate accounting.

For example, a joint operator would recognise its share of an asset in accordance with IAS 16 *Plant, Property and Equipment*, or IAS 38 *Intangible Assets*, as applicable. When the contractual terms of the joint operation provide a joint operator with a right to use an asset, not a share of the asset itself, the joint operator would apply IFRIC 4 *Determining Whether an Arrangement Contains a Lease*.

6.3 Parties to a joint operation without joint control

In some cases, a party is involved in a joint operation, but does not have joint control. That is, it is not a joint operator. IFRS 11 states that to the extent that party has rights to assets and obligations for liabilities, the accounting is the same as that for a joint operator, as discussed above.

If the party does not have rights to the assets and obligations for the liabilities relating to the joint operation, it accounts for its interest in the joint operation in accordance with other relevant IFRS. For example, if it has:

- ▶ An interest in a separate vehicle over which it has significant influence – apply IAS 28
- ▶ An interest in a separate vehicle over which it does not have significant influence – account for that interest as a financial asset
- ▶ An interest in an arrangement without a separate vehicle – apply other applicable IFRS

Effectively, if the joint arrangement is a joint operation, and the party has rights to the assets and obligations for the liabilities relating to that joint operation, it does not matter whether the parties to that joint arrangement have joint control or not – the accounting is the same.

However, the disclosure requirements will differ as IFRS 12 does not apply to joint arrangements in which a party does not have joint control, unless that party has significant influence. Disclosure requirements are discussed in Section 9.

6.4 Joint operations with a non-controlling interest/passive investor

Since a joint operation may be conducted through a separate vehicle, there may be a party to the joint operation that has an ownership interest in that separate vehicle, but does not have joint control (i.e., a passive investor).

In such cases, a joint operator does not recognise the rights to assets and obligations for the liabilities attributable to the non-controlling interest/passive investor, or recognise a non-controlling interest. Rather, a joint operator only recognises its share of any assets held jointly and its obligations for its share of any liabilities incurred jointly. This is shown in Example 15.

Example 15 – Joint operation with a non-controlling interest passive investor

A and B enter into a joint operation, Z, which is contained in a separate vehicle. Each of the two entities owns 40% of the shares of the separate vehicle. The remaining 20% of Z is owned by C, but C does not have joint control over Z, as C is not party to the joint arrangement. C is considered a passive investor and accounts for its interest in the arrangement to the extent it has rights to the assets and obligations for the liabilities. The legal form of the separate vehicle does not confer separation between the parties and the separate vehicle itself. That is, A and B have rights to the assets and obligations for the liabilities of Z (therefore, Z is a joint operation). Neither the contractual terms, nor the other facts and circumstances indicate otherwise. Accordingly, A, B and C recognise their assets, including their share of any assets held jointly, and their liabilities, including their share of any liabilities incurred jointly, in accordance with the relevant IFRS.

In A's financial statements, it recognises its assets, liabilities, revenues and expenses in Z, which would be 40% of Z's assets, liabilities, revenues and expenses in accordance with the relevant IFRS. A does not recognise a non-controlling interest related to Z.

6.5 Transactions between a joint operator and a joint operation

IFRS 11 addresses transactions between a joint operator and a joint operation.

Excerpt from IFRS 11

- B34 When an entity enters into a transaction with a joint operation in which it is a joint operator, such as a sale or contribution of assets, it is conducting the transaction with the other parties to the joint operation and, as such, the joint operator shall recognise gains and losses resulting from such a transaction only to the extent of the other parties' interests in the joint operation.
- B35 When such transactions provide evidence of a reduction in the net realisable value of the assets to be sold or contributed to the joint operation, or of an impairment loss of those assets, those losses shall be recognised fully by the joint operator.
- B36 When an entity enters into a transaction with a joint operation in which it is a joint operator, such as a purchase of assets, it shall not recognise its share of the gains and losses until it resells those assets to a third party.
- B37 When such transactions provide evidence of a reduction in the net realisable value of the assets to be purchased or of an impairment loss of those assets, a joint operator shall recognise its share of those losses.

How we see it

When there is a transaction between a joint operator and a joint operation, consideration should be given to whether the transaction changes the nature of the joint operator's rights to assets, or obligations for liabilities. Any such changes should be reflected in the joint operator's financial statements, and the new assets and liabilities should be accounted for in accordance with the relevant IFRS.

Although these requirements do not specifically refer to parties to a joint operation who do not have joint control (e.g., passive investors in the joint operation), we believe it would be appropriate to use the same accounting in such circumstances.

7. Accounting for joint ventures

If an entity has joint control over a joint venture, it must apply the equity method of accounting in accordance with IAS 28. All assets, liabilities, revenues and expenses of these entities will net into one unit of accounting, 'investment in joint venture', and the entity will recognise its share of the joint venture's net income and changes in equity. As discussed in Section 2.1, venture capital organisations can choose to measure investments in joint ventures at fair value. This is a measurement exemption under IFRS 11, rather than a scope exemption, which means that such entities are subject to the disclosure requirements for joint ventures, as discussed in Section 9.

7.1 Interest in a joint venture without joint control

IAS 28 is applied if an investor does not have joint control over a joint venture, but has significant influence over an entity. However, the disclosure requirements under IFRS 12 will differ.

If the investor has significant influence, but the joint venture is not an entity (i.e., it is a separate vehicle, such as a silo), IAS 28 would not apply, and the investor would apply the relevant IFRS.

If an investor does not have significant influence, its interest in the joint venture would be accounted for as a financial asset.

7.2 Contributions of non-monetary assets to a joint venture

When an entity contributes a non-monetary asset or liability to a joint venture in exchange for an equity interest in the joint venture, it recognises the portion of the gain or loss attributable to the other parties to the joint venture except when the contribution lacks commercial substance.

However, when the contributed non-monetary asset is a subsidiary of an entity, a conflict arises between the requirements of IAS 28 and IFRS 10. This is discussed in Section 8.2.3.

8. Continuous assessment

If facts and circumstances change, IFRS 11 requires a party to reassess whether:

- ▶ It still has joint control of the arrangement
- ▶ The type of joint arrangement has changed

8.1 When to reassess under IFRS 11

IFRS 11 does not contain any specific points at which a party reassesses whether it has joint control, or the type of joint arrangement. Accordingly, a party reassesses upon any change in facts and circumstances that might be relevant to those conclusions. In some cases, changes in facts and circumstances might result in a party having control over the arrangement (which would, therefore, no longer be a joint arrangement since one party has control). In other cases, an arrangement may remain under joint control, but the classification might change from joint venture to joint operation (or vice versa). A careful evaluation is needed based on the facts and circumstances in each case.

Reassessment of a joint arrangement should occur upon a change in:

- ▶ *How activities are directed* – For example, A set up Z to develop a new product or technology. Initially, Z had a Board of Directors elected by shareholders and the relevant activities were directed by voting rights held exclusively by A. If A enters into an agreement with B so that A and B must agree on all decisions (e.g., they replace the Board, and make decisions for management), reassessment would be required to evaluate whether A and B have joint control of Z.
- ▶ *Legal form* – For example, a separate vehicle that initially did not confer separation between the parties and the vehicle (e.g., a general partnership) is converted into a separate vehicle that now does confer separation between the parties and the vehicle (e.g., a limited partnership). Reassessment would be required to evaluate whether this indicates a change in classification from a joint operation to a joint venture.
- ▶ *Contractual terms* – For example, the terms of a joint arrangement are renegotiated, such that the parties have rights to the assets, or obligations for the liabilities. Reassessment would be required to evaluate whether this indicates a change in classification to a joint operation.
- ▶ *Other facts and circumstances* – For example, the terms and conditions of a joint operation are renegotiated. Initially, a joint arrangement could sell output only to the parties of the joint arrangement. Subsequently, the joint arrangement may also sell output to third-party customers. Reassessment would be required to evaluate whether this indicates a change in classification from joint operation to a joint venture.

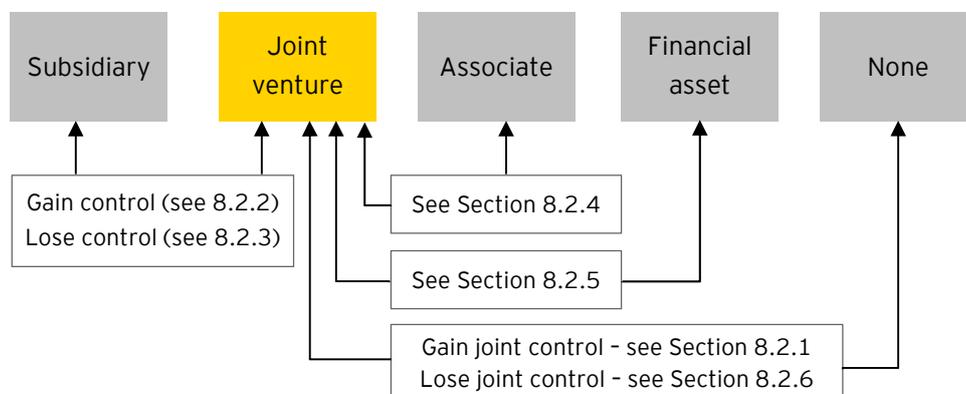
As discussed in Section 5.3.1, another event that might trigger reassessment would be an event that leads a guarantor to have to pay (or perform) under a guarantee.

8.2 Changes in ownership with respect to a joint venture

The accounting for changes in ownership with respect to a joint venture depends on the type of interest held before the change in ownership occurred. In Section 8.2.1, we discuss acquisitions in a joint venture where no previous interest was held. In the remainder of this section, we discuss changes to a pre-existing interest. Diagram 9 illustrates the possible changes with respect to a joint venture.

Diagram 9 – Changes in ownership with respect to a joint venture

The discussion of the accounting for a change in ownership interest with respect to a joint venture is indicated in the box linking the type of interest held before and after a change in ownership.



8.2.1 Acquisition of an interest in a joint venture

The accounting for the acquisition of an interest in a joint venture is accounted for as described in IAS 28. This is covered in more detail in Chapter 11 of *International GAAP® 2014*.

8.2.2 Control over a former joint venture

If an entity gains control over a former joint venture, it applies IFRS 3, provided that the acquiree meets the definition of a business. Otherwise, the entity applies paragraph 2(b) of IFRS 3 and measures the assets on a relative fair value basis. Additional information regarding the application of IFRS 3 can be found in Chapter 9 of *International GAAP® 2014*.

8.2.3 Former subsidiary becomes a joint venture

When a subsidiary becomes a joint venture, there is a conflict between the requirements of IAS 28 and IFRS 10 on how to calculate any gain or loss arising in this transaction. This conflict arises when a parent contributes a subsidiary to a joint venture (or loses control over a subsidiary, which then becomes a joint venture), and receives an ownership interest in that joint venture in exchange. This may occur, for example, if a parent sells shares in a subsidiary to another party and the arrangement becomes a joint venture, or by dilution (i.e., if the subsidiary issues new shares to another party and the arrangement becomes a joint venture).

If IFRS 10 is applied, when an entity loses control of a subsidiary, and obtains joint control of a joint venture, the entity will:

- ▶ Derecognise the assets and liabilities of the former subsidiary (including any related goodwill and non-controlling interests) from the consolidated statement of financial position
- ▶ Recognise the fair value of any consideration received
- ▶ Recognise any distribution of shares in the subsidiary to owners
- ▶ Recognise the retained investment in the joint venture at its fair value when control is lost and subsequently account for it in accordance with IFRS 11 and IAS 28 (the fair value is deemed its cost under the equity method)

- ▶ Reclassify to profit or loss, or to retained earnings (based on the applicable IFRS) amounts recognised in other comprehensive income related to that subsidiary
- ▶ Recognise the resulting gain or loss without restriction (i.e., the full gain or loss would be recognised)

In contrast, if IAS 28 is applied, this will limit the gain recognised when a subsidiary is contributed to a joint venture to the portion attributable to the other parties to the joint venture. To address this conflict, in December 2012 the IASB issued an Exposure Draft (ED) *Sale or Contribution of Assets between an Investor and its Associate or Joint Venture*, which proposes to amend IFRS 10 so that the gain or loss on transactions that do not constitute a business is recognised only to the extent of the unrelated investors interests in the joint venture where the sale or contribution of assets does constitute a business, the gain or loss would be recognised in full. The IASB intends to issue an amendment later in 2014.

To determine the fair value of the retained investment in the joint venture, an entity applies IFRS 13 *Fair Value Measurement*. However, IFRS 13 does not specify whether the unit of account for investments in subsidiaries, joint ventures and associates is the investment as a whole or the individual financial instruments that make up the investment. At its meeting in March 2013, the IASB tentatively decided that the unit of account for investments in subsidiaries, joint ventures and associates is the investment as a whole. The IASB also tentatively decided that the fair value measurement of an investment comprised of financial instruments quoted in an active market, should be the product of the quoted price of the financial instrument (P) multiplied by the quantity (Q) of instruments held (i.e., $P \times Q$). The IASB expects to issue an exposure draft clarifying the fair value measurement of quoted investments in subsidiaries, joint ventures and associates, during 2014.

8.2.4 Joint venture becomes an associate (or vice versa)

If a joint venturer loses joint control, but retains an interest in an associate, it would continue to apply the equity method. However, an entity does not remeasure its retained interest in an associate when it loses joint control over a joint venture. Similarly, the entity does not reclassify any amounts previously recognised in other comprehensive income and accumulated in equity (e.g., foreign currency translation adjustments).

In the Basis for Conclusions to IAS 28, the IASB acknowledged that the nature of the investor-investee relationship changes upon changing from joint venture to associate (or vice versa). However, since the investment continues to be accounted for using the equity method (i.e., there is no change in the measurement requirements), and there is no change in the group, it is not an event that warrants re-measurement of the retained interest at fair value.

8.2.5 Joint venture becomes a financial asset

If a joint venture becomes a financial asset the measurement method changes. The entity measures the retained interest in the financial asset at fair value, which becomes its fair value on initial recognition as a financial asset.

The entity recognises in profit or loss any difference between:

- ▶ The fair value of any retained interest and any proceeds from disposing of a part interest in the joint venture

And

- ▶ The carrying amount of the interest in the joint venture at the date the equity method was discontinued

If a gain or loss previously recognised by the entity in other comprehensive income would be reclassified to profit or loss on the disposal of the related assets or liabilities, IAS 28 requires the entity to reclassify the gain or loss from equity to profit or loss when the equity method is discontinued. For example, gains and losses related to foreign currency translation adjustments accumulated in equity would be reclassified to profit or loss. The requirements of IAS 28 are discussed in more detail in Chapter 11 of *International GAAP*® 2014.

Alternatively, a financial asset may become a joint venture by acquisitions of further interests. IAS 28 is unclear on how piecemeal acquisitions of a joint venture should be treated. This is discussed further in Chapter 11 of *International GAAP*® 2014.

8.2.6 Disposal of interest in a joint venture

When an entity disposes of its interest in a joint venture, it ceases to use the equity method as of that date. It also de-recognises its interest and recognises any gain or loss upon sale.

In such cases, an entity cannot restate its financial statements for the period (or the comparative period) as if it did not have joint control during the reporting period. IAS 28 requires that the entity uses the equity method up to the date that the joint venturer disposes of its interest in the joint venture. This assumes that the entity is not exempt from preparing financial statements by IFRS 10, IAS 27 or IAS 28, and that it is not using the fair value measurement exemption (see Section 2.1).

8.2.7 Interest in a joint venture held for sale

When a joint venturer plans to dispose of its entire interest in a joint venture, it applies IFRS 5 *Non-current Assets Held for Sale and Discontinued Operations*. When a joint venturer plans to dispose of part of an interest in a joint venture, it reclassifies only the interest to be disposed of as held for sale, when that portion meets the criteria for classification as held for sale. The joint venturer continues to account for the retained interest in the joint venture using the equity method until the disposal of that interest occurs. This is because an entity continues to have joint control over its entire interest in the joint venture until it actually disposes of that interest (and not before). Upon disposal, it reassesses the nature of its interest and accounts for that interest accordingly (e.g., as a financial asset).

If an interest (or a portion of an interest) in a joint venture no longer meets the criteria to be classified as held for sale, the interest is accounted for using the equity method retrospectively from the date of its classification as held for sale.

8.3 Changes in ownership with respect to a joint operation

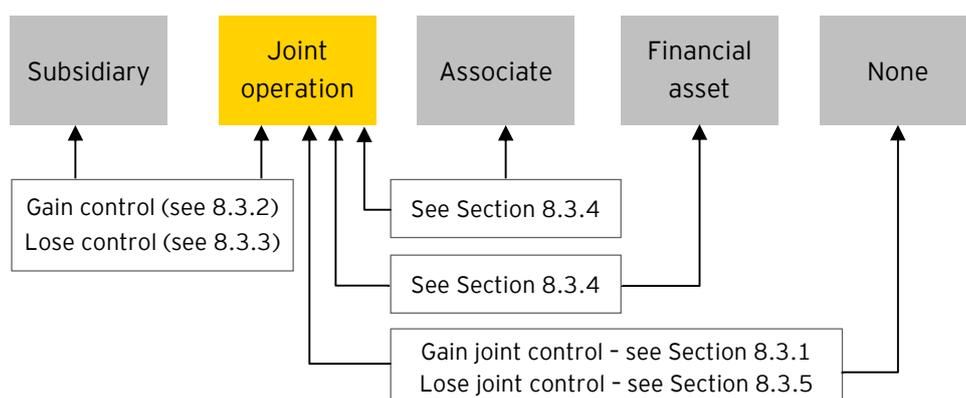
The accounting for changes in ownership with respect to a joint operation depends on the type of interest held previously. In Section 8.3.1, we discuss acquisitions in a joint operation where no previous interest was held. In the remainder of this section, we discuss changes to an existing interest. Diagram 11 illustrates the possible changes with respect to a joint operation.

8.3.1 Acquisition of an interest in a joint operation

The IASB issued an amendment to IFRS 11 *Acquisitions of Interests in Joint Operations* in May 2014. The amendment requires that a joint operator accounting for the acquisition of an interest in a joint operation in which the activity of the joint operation constitutes a business, must apply the relevant principles for business combination accounting in IFRS 3 and disclose the information required for business combinations. The amendment is effective for annual periods beginning on or after 1 January 2016, although early application is permitted.

Diagram 10 – Changes in ownership interest with respect to a joint operation

The discussion of the accounting for a change in ownership interest with respect to a joint operation is indicated in the box linking the type of interest held before and after a change of ownership.



How we see it

The drafting in IFRS 3 and IFRS 11 is not clear. The accounting method selected by management should be appropriate based on the facts and circumstances of the transaction. Parties that acquire an interest in a joint operation should monitor discussions by the Interpretations Committee and/or the IASB, if applicable.

8.3.2 Control over a former joint operation

If an entity gains control over a former joint operation that meets the definition of a business, it applies the accounting for business combinations in IFRS 3. Otherwise, the entity applies paragraph 2(b) of IFRS 3 and measures the acquired assets and liabilities on a relative fair value basis. Additional information regarding the application of IFRS 3 can be found in Chapter 9 of *International GAAP*® 2014.

8.3.3 Former subsidiary becomes a joint operation

As stated in IFRS 10, if an entity loses control of a subsidiary and gains joint control of a joint operation, the entity will generally:

- ▶ Derecognise the assets and liabilities of the former subsidiary (including any related goodwill and non-controlling interests) from the consolidated statement of financial position
- ▶ Recognise the fair value of any consideration received
- ▶ Recognise any distribution of shares of the subsidiary to owners
- ▶ Recognise the rights to the assets and obligations for the liabilities of the joint operation at fair value (as noted in Section 8.3.1, it is not clear whether IFRS 3 applies in this case)
- ▶ Reclassify to profit or loss, or to retained earnings (based on the applicable IFRS) amounts recognised in other comprehensive income related to that subsidiary
- ▶ Recognise the resulting gain or loss

The above accounting is the same as the approach used when a former subsidiary becomes a joint venture, and the IFRS 10 approach is used (see Section 8.2.3). The other approach referred to in Section 8.2.3 (the IAS 28 approach) would not be available in this situation, because IAS 28 does not apply to joint operations.

8.3.4 Other changes in ownership of a joint operation

IFRS 11 does not explicitly address the accounting for a former joint operation, and the situation in which it becomes an associate, financial instrument, or it is replaced by control of individual assets or liabilities.

In accordance with IFRS 5, when a joint operator plans to dispose of part of an interest in a joint operation, it reclassifies only the interest to be disposed of as held for sale, when that portion meets the criteria for classification as held for sale. The joint operator continues to account for the retained interest in the joint operation in accordance with IFRS 11 until the disposal of that interest occurs. This is because an entity continues to have joint control over its entire investment in the joint operation until it actually disposes of that interest. Upon disposal, it then reassesses the nature of its remaining interest and accounts for that interest accordingly (e.g., as an associate or financial asset).

If an interest (or a portion of an interest) in a joint operation no longer meets the criteria to be classified as held for sale, an entity restates the financial statements for the periods since classification as held for sale.

How we see it

When a former joint operation becomes an associate (this would only be the case where there is an entity) or financial instrument, it would generally be appropriate to de-recognise the assets and liabilities previously recognised in accordance with IFRS 11 and account for the new interest based on the applicable IFRS at that date. This approach may also be appropriate when the rights to assets or obligations for liabilities held by the entity when it was a joint operation differ from those that it has rights to or obligations for when it ceases to have an interest in a joint operation.

However, when an entity's rights to assets and obligations for liabilities are the same both within the joint operation, and after the entity ceases to have an interest in the joint operation, we generally would not expect a change in the accounting.

8.3.5 Disposal of interest in a joint operation

When an entity disposes of its interest in a joint operation, it ceases to account for the rights to assets and obligations for liabilities, and recognises any gain or loss as of the disposal date. The only exception would be if rights to assets or obligations for liabilities replaced that interest directly. In this case, there would be no change in accounting, because, in both cases, the assets and liabilities are recognised in accordance with the relevant IFRS.

Consistent with the treatment of joint ventures, as noted in Section 8.2.6, an entity continues to reflect its interest in a joint operation for the reporting period (and comparative period) in which it held that interest. An entity does not restate its financial statements as if it never held the interest in the disposed joint operation.

8.4 Changes from a joint operation to a joint venture

IFRS 11 does not explicitly address the accounting for a former joint operation that becomes a joint venture, (other than at transition).

8.4.1 Joint operation becomes a joint venture

When a former joint operation becomes a joint venture, it is generally appropriate to de-recognise the assets and liabilities previously recognised in accordance with IFRS 11 and account for the new interest in the joint venture in accordance with IAS 28. IAS 28 is covered in more detail in Chapter 11 of *International GAAP® 2014*.

8.4.2 Joint venture becomes a joint operation

When a former joint venture becomes a joint operation, it is appropriate to de-recognise the equity method investment and account for the rights to assets and obligations for liabilities as of the date of the change in accordance with IFRS 11 (see Section 6).

9. Disclosures

IFRS 12 contains the disclosure requirements for an entity's interests in joint arrangements. The disclosure requirements described here are those that apply to parties that have joint control of the joint arrangement; they do not apply to passive investors in a joint arrangement (i.e., parties without joint control). However, if a party has significant influence over the joint arrangement, the disclosure requirements in IFRS 12 with respect to associates would apply, although they differ slightly from those described below. In such cases, reference should be made to *International GAAP*[®], and *Disclosure Checklist* and *Good Group Illustrative Financial Statements*.

Disclosure requirements in IFRS 12 related to subsidiaries, including consolidated and unconsolidated structured entities are discussed in our publication, *Applying IFRS 10*, Section 11.

9.1 Principles of IFRS 12

The objective of IFRS 12 is for an entity to disclose information that helps users of its financial statements evaluate:

- ▶ The nature of, and risks associated with, its interests in other entities, including the contractual relationship with the other parties that have joint control
- ▶ The effects of those interests on its financial position, financial performance, and cash flows

These are discussed in Sections 9.2 – 9.6. Related party transactions are discussed in Section 9.7.

Excerpt from IFRS 12

- 3 If the disclosures required by this IFRS, together with disclosures required by other IFRSs, do not meet the objective in paragraph 1 [summarised above], an entity shall disclose whatever additional information is necessary to meet that objective.
- 4 An entity shall consider the level of detail necessary to satisfy the disclosure objective and how much emphasis to place on each of the requirements in this IFRS. It shall aggregate or disaggregate disclosures so that useful information is not obscured by either the inclusion of a large amount of insignificant detail or the aggregation of items that have different characteristics.

How we see it

Management will need to use judgement to meet the disclosure objectives of IFRS 12. Notwithstanding the specific requirements of IFRS 12, an entity may need to disclose additional information to meet the objectives above.

9.2 Disclosing judgements

An entity must disclose the significant judgements and assumptions it has made (and changes thereto) in determining whether or not it has joint control of an arrangement. An entity is also required to disclose significant judgements made in determining the type of joint arrangement (i.e., joint operation or joint venture) when the arrangement is structured through a separate vehicle.

The requirements in IFRS 12 reflect the degree of judgement that is required to determine whether an entity has joint control. The following are examples of significant judgements for which disclosure may be required:

- ▶ Whether a right is a protective right (which does not give joint control) or a substantive right that gives an entity joint control
- ▶ Whether a manager of an arrangement is acting as principal or as agent, which would likely affect the conclusion as to whether the manager has control or joint control
- ▶ Whether a joint arrangement is a joint operation or a joint venture, since its classification is not merely based on legal form under IFRS 11.

9.3 Nature of an entity's interest in a joint arrangement

IFRS 12 requires that for each joint arrangement that is material to the entity, the entity must disclose all of the following:

- ▶ Name of the joint arrangement
- ▶ Nature of the entity's relationship with the joint arrangement (by, for example, describing the nature of the activities of the joint arrangement and whether they are strategic to the entity's activities)
- ▶ Principal place of business (and country of incorporation, if applicable and different from the principal place of business) of the joint arrangement
- ▶ Proportion of ownership interest or participating share held by the entity and, if different, the proportion of voting rights held (if applicable)

The above requirements apply both to joint operations and joint ventures. Example 16 illustrates these disclosures.

Example 16 – Nature of joint arrangement

The Group has a 50% ownership interest in F Limited, a joint arrangement, which is held by its subsidiary, K Limited. F Limited's principal place of operations is Eurasia, but it is incorporated in Delaware in the United States. K Limited is one of two partners in this joint arrangement, the purpose of which is to extract gas reserves from fields in Eurasia. F Limited is a supplier of gas in Eurasia. F Limited is strategic to the Group's business, given the similarity in business lines to the Group's operations.

9.4 Nature, extent and financial effects of an entity's interest in a joint venture

In addition to the information above, an entity is required to disclose additional information about interests in joint ventures. The table in Diagram 11 summarises the disclosures required for material joint ventures, the disclosures required for immaterial joint ventures (in the aggregate), and the disclosures required for both. The requirements are discussed in more detail in the remainder of this section. The disclosures in Diagram 11 are not required for joint operations.

Diagram 11 – Required disclosures for joint ventures

Topic	Individually material joint ventures	Individually immaterial joint ventures
Accounting policy (i.e., equity method or fair value)	✓	X
Summarised financial information	✓	✓ (in aggregate and less granular)
Fair value, if quoted market price is available and measured using the equity method	✓	X
Restrictions on ability to transfer funds	✓	✓
Date of financial statements, if different from entity, and reason for different date	✓	✓
Unrecognised share of losses at financial statement date and cumulatively	✓	✓

✓ Required

X Not required

How we see it

As shown in Diagram 11, IFRS 12 does not exclude immaterial joint ventures from the disclosure requirements related to restrictions on its ability to transfer funds, the date of the financial statements of the joint venture, or the unrecognised share of losses. However, IAS 1 *Presentation of Financial Statements* should also be considered, which states that an entity is not required to comply with the specific disclosure requirements of an IFRS, if the information is not material. Evaluating which information may be useful to users of the financial statements will require judgement.

9.4.1 Accounting policy for material joint ventures

For material joint ventures, an entity is required to disclose the accounting policy used to account for that joint venture. Although this is typically the equity method, in some cases, an entity may use fair value (see Section 2.1).

If fair value is used to measure the investment in the joint venture, or if fair value is disclosed, consideration should also be given to the requirements of IFRS 13 *Fair Value Measurement*. For example, IFRS 13 requires the significant inputs to be disclosed when a fair value measurement is used in the financial statements, and requires the level within the fair value hierarchy to be disclosed.

9.4.2 Summarised financial information

An entity is required to disclose summarised financial information for joint ventures. IFRS 12 requires information for each joint venture that is material to the entity, and summarised information in the aggregate for individually immaterial joint ventures. However, the scope of the required information varies between the two, as shown in Diagram 12. It should be noted that, to meet the objective of IFRS 12, a joint venturer may need to disclose additional information beyond those items listed in Diagram 12.

Diagram 12 – Summarised financial information for joint ventures

	Joint ventures (individually material)	Joint ventures (individually immaterial)
Amount disclosed	Entire amount (i.e., 100%)	Joint venturer's share
Dividends received	√	X
Carrying amount of investment	√	X
Cash and cash equivalents included in current assets	√	X
Current assets	√	X
Non-current assets	√	X
Current financial liabilities excluding trade payables and other provisions included in current liabilities	√	X
Current liabilities	√	X
Non-current financial liabilities excluding trade payables and other provisions included in current liabilities	√	X
Non-current liabilities	√	X
Revenue	√	X
Depreciation and amortisation	√	X
Interest income	√	X
Interest expense	√	X
Income tax expense or income	√	X
Profit or loss from continuing operations	√	√
Post-tax profit or loss from discontinued operations	√	√
Other comprehensive income	√	√
Total comprehensive income	√	√

When the joint venturer accounts for the joint venture using the equity method, the individual summarised financial information for a material joint venture is adjusted to reflect adjustments made by the joint venturer when using the equity method. For example, this might include:

- ▶ Fair value adjustments made at the time of acquisition
- ▶ Adjustments for differences in accounting policies

The joint venturer is also required to disclose a reconciliation between the summarised financial information and the carrying amount of its interest in the joint venture. IFRS 12 does not specify which components should be included in the reconciliation. Therefore, a joint venturer should disclose components that are meaningful (and material) to users of the financial statements. For example, these may include goodwill and other fair value adjustments recognised in the notional purchase price allocation under the equity method.

It should be noted that a joint venturer would include its goodwill arising on the acquisition of the joint venture within the summarised financial information for a material joint venture. However, this is the joint venturer's own goodwill attributable to its interest in the joint venture. The goodwill attributable to interests in the joint venture held by other joint venturers are presumably not known. Therefore, care will be needed in presenting any such goodwill and in explaining the nature of this goodwill in the reconciliation. In addition, any goodwill recorded in the financial statements of the joint venture itself would presumably be reflected as a fair value adjustment by the joint venturer upon acquisition of its interest in the joint venture.

The above requirements are illustrated in Example 17.

Summarised information is also required if the fair value option is used to account for investments in associates and joint ventures (by venture capital organisations). However, this information is not required to be presented in accordance with IFRS if both of the following criteria are met:

- ▶ The joint venture does not prepare IFRS financial statements
- ▶ Preparation on that basis would be impracticable or cause undue cost ('impracticable' is defined in IAS 8 *Accounting Policies, Changes in Accounting Estimates and Errors*)

That is, if both of the above criteria are met, the summarised financial information may be presented on a non-IFRS basis, when the fair value option is used.

When a joint venture accounted for at fair value does prepare IFRS financial statements, or where the preparation of IFRS financial information would not be impracticable or cause undue cost, the summarised financial information disclosed is that of the joint venture in its IFRS financial statements, on an unadjusted basis.

Summarised information is not required when a joint venture (or a portion of an interest therein) is classified as held-for-sale by the joint venturer in accordance with IFRS 5 (although the disclosure requirements of IFRS 5 would then apply). However, this should not be confused with the situation where the joint venture itself has assets held for sale in accordance with IFRS 5, in which case, summarised financial information for the joint venture is still required.

Example 17 – Summarised financial information

In the example below, F Limited and G Inc. are material joint ventures to the Group. It is assumed that there are no discontinued operations and that the Group has a 50% ownership interest in F Limited and a 35% interest in G Inc.

Note X – Investments in joint ventures (in CUs)	20X2	20X1
F Limited	4,150	4,025
G Inc	3,705	3,670
Other joint ventures	300	290
Total investments in joint ventures	8,155	7,985
<i>Movement in investment in joint ventures during the reporting period</i>		
Balance at beginning of the reporting period	7,985	7,732
Share of total comprehensive income	290	245
Dividends received	(50)	(57)
Exchange and other adjustments	(70)	65
Balance at end of the reporting period	8,155	7,985
<i>Share of comprehensive income from joint ventures</i>		
<i>Profit after tax from continuing operations</i>		
F Limited ⁷	225	188
G Inc ⁷	34	28
Other joint ventures ⁸	7	11
Total share of profit after tax from continuing operations from joint ventures⁹	266	227
<i>Other comprehensive income</i>		
F Limited ⁷	20	17
G Inc ⁷	2	(1)
Other joint ventures ⁸	2	2
Total share of other comprehensive income from joint ventures⁹	24	18
<i>Other comprehensive income</i>		
F Limited ⁷	245	205
G Inc ⁷	36	27
Other joint ventures ⁸	9	13
Total share of comprehensive income from joint ventures⁹	290	245

⁷ Neither IFRS 12 nor IAS 1 requires a joint venturer to show the joint venturer's share of profits or comprehensive income from individually material joint ventures. However, to meet the objective of IFRS 12 and to assist in this reconciliation, joint venturers are encouraged to disclose their share of profits and comprehensive income from individually material joint ventures.

⁸ IFRS12 requires disclosure of the share of profit and other comprehensive income from immaterial joint ventures in aggregate.

⁹ IAS 1 requires disclosure of the total share of profit and comprehensive income.

Example 17 – Summarised financial information (continued)

Summarised statement of financial position	20X2 F Limited	20X1 F Limited	20X2 G Inc	20X1 G Inc
Cash and cash equivalents	200	850	200	250
Other current assets	300	200	200	100
Total current assets	500	1,050	400	350
Non-current assets, excluding goodwill	9,800	9,023	5,400	5,222
Goodwill	1,725	1,725	2,546	2,546
Total assets	12,025	11,798	8,346	8,168
Current financial liabilities (excluding trade, other payables and provisions)	200	180	100	120
Other current liabilities	200	250	350	300
Total current liabilities	400	430	450	420
Non-current financial liabilities (excluding trade, other payables and provisions)	5,000	5,000	2,000	2,100
Other non-current liabilities	50	43	40	40
Total non-current liabilities	5,050	5,043	2,040	2,140
Total liabilities	5,450	5,473	2,490	2,560
Net assets	6,575	6,325	5,856	5,758
Net assets, excluding goodwill	4,850	4,600	3,310	3,212

Summarised statement of comprehensive income	20X2 F Limited	20X1 F Limited	20X2 G Inc	20X1 G Inc
Revenue	2,500	1,500	750	650
Depreciation and amortisation	200	180	100	110
Interest income	25	20	60	55
Interest expense	180	200	75	85
Profit/(loss) before tax	600	500	130	110
Income tax expense	(150)	(125)	(33)	(28)
Profit/(loss) after tax	450	375	97	82
Other comprehensive income	40	35	5	(4)
Total comprehensive income	490	410	102	78

Reconciliation of share of net assets to carrying amount	20X2 F Limited	20X1 F Limited	20X2 G Inc	20X1 G Inc
Group share of net assets of joint venture, excluding goodwill	2,425	2,300	1,589	1,124
Goodwill on acquisition less cumulative impairment	1,725	1,725	2,546	2,546
Carrying amount of investment in joint venture	4,150	4,025	3,705	3,670

9.4.3 Fair value for joint ventures with quoted market prices

IFRS 12 requires disclosure of the fair value of a joint venturer's investment in a material joint venture that is accounted for using the equity method, if there is a quoted market price for that investment. When fair value is disclosed, consideration should also be given to the requirements of IFRS 13, which applies even though the entity is using the equity method (although the disclosure requirements are less than if fair value had been used).

9.4.4 Restrictions on joint ventures

A joint venturer is required to disclose the nature and extent of any significant restrictions on:

- ▶ The ability of the joint venture to transfer funds to the joint venturer in the form of cash dividends
- Or
- ▶ To repay loans or advances made by the joint venturer

For example, restrictions might result from covenants under borrowing arrangements with third parties, regulatory requirements or contractual arrangements between joint venturers.

9.4.5 Date of financial statements for applying equity method

When the financial statements of a joint venture used in applying the equity method are as of a date or for a period that is different from that of the joint venturer, the joint venturer is required to disclose both:

- ▶ The date of the end of the reporting period of the financial statements of that joint venture or associate
- ▶ The reason for using a different date or period

9.4.6 Unrecognised losses

A joint venturer may have stopped recognising its share of losses of the joint venture when applying the equity method (e.g., because the investment has been reduced to nil due to recognition of past losses, and there is no commitment to finance such losses). In such cases, the joint venturer is required to disclose its unrecognised share of losses of a joint venture, both for the reporting period and cumulatively.

9.5 Risks associated with interests in joint ventures

One of the objectives for the disclosures for joint arrangements relates to the nature of, and changes in, risks related to that joint venture. To meet this objective, a joint venturer is required to disclose:

- ▶ Commitments that it has relating to its joint ventures, separately from the amount of other commitments
- ▶ Contingent liabilities incurred relating to its interests in joint ventures, separately from the amount of other contingent liabilities

These are discussed in further detail in the remainder of Section 9.5. These disclosure requirements apply only to joint ventures.

9.5.1 Commitments relating to interests in joint ventures

A joint venturer is required to disclose total commitments it has made, but not recognised at the reporting date relating to its interests in joint ventures. This amount includes its share of commitments made jointly with other joint venturers. A commitment is anything that may give rise to a future outflow of cash or other resources.

IFRS 12 lists several examples of items that may create an unrecognised commitment to contribute funding or resources:

- ▶ Constitution or acquisition agreements of the joint venture (e.g., those that require an entity to contribute funds over a specific period)
- ▶ Capital-intensive projects undertaken by a joint venture
- ▶ Unconditional purchase obligations, comprising procurement of equipment, inventory or services that the joint venturer is committed to purchasing from, or on behalf of, a joint venture
- ▶ Commitments to provide loans or other financial support to a joint venture
- ▶ Commitments to contribute resources to a joint venture, such as assets or services

A joint venturer may also have an unrecognised commitment to acquire another party's ownership interest (or a portion of that ownership interest) in a joint venture upon a contingent event (or lack thereof).

9.5.2 Contingent liabilities with respect to joint ventures

A joint venturer is required to disclose contingent liabilities incurred relating to its interests in joint ventures, separately from the amount of other contingent liabilities.

This disclosure must be in accordance with IAS 37, which requires disclosure of the following, unless the probability of loss is remote:

- ▶ An estimate of the contingent liability
- ▶ An indication of the uncertainties relating to the amount or timing of any outflow
- ▶ The possibility of any reimbursement

The contingent liability disclosed related to joint ventures includes a joint venturer's share of contingent liabilities incurred jointly with other joint venturers or investors that have significant influence over the joint venture.

9.6 Joint arrangements that are structured entities

It is possible that a joint arrangement will meet the definition of a structured entity. When this occurs, the disclosure requirements in IFRS 12 for unconsolidated structured entities would apply. This would also be the case if a party has significant influence over an associate, and that associate meets the definition of a structured entity. While the IASB only refers to joint ventures and associates in its discussion of this point (in the Basis for Conclusions to IFRS 12), the same could also be true for a joint operation.

Excerpt from Appendix A to IFRS 12

Structured entity – An entity that has been designed so that voting or similar rights are not the dominant factor in deciding who controls the entity, such as when any voting rights relate to administrative tasks only and the relevant activities are directed by means of contractual arrangements.

The definition of a structured entity and the related disclosure requirements are discussed in more detail in our publication, *Applying IFRS 10*, Sections 4.4.1, and 11.4, respectively.

9.7 Related party transactions

IFRS 12 notes that the disclosures required in relation to the risks associated with the joint venturer's interest in its joint venture (discussed in Section 9.5) include some of the types of disclosures required under IAS 24 *Related Party Disclosures*. Below, we summarise the disclosure requirements for joint arrangements (including joint operations) in IAS 24.

9.7.1 Scope of related party disclosure requirements

IAS 24 requires disclosure of related party relationships, transactions and outstanding balances, including commitments, in consolidated, separate or individual financial statements of:

- ▶ The parent
- ▶ The joint venturer
- ▶ The joint operator
- ▶ An investor with significant influence over an investee

This is consistent with the previous requirements.

9.7.2 Persons or close family members that are related parties

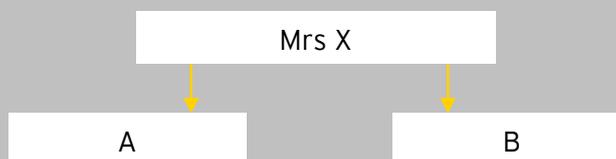
A person or close family member of that person is related to a reporting entity if that person:

- ▶ Has control or joint control of the reporting entity
 - ▶ Has significant influence over the reporting entity
- Or
- ▶ Is a member of the key management personnel of the reporting entity or of a parent of the reporting entity

Transactions with such parties are considered related party transactions, and are required to be disclosed. The definition of joint control is the same in IAS 24 and IFRS 11. The disclosure applies to both joint ventures and joint operations because of the reference to joint control.

Business relationships that involve an individual or close family member are illustrated in Examples 18 and 19, which are based on illustrative examples in IAS 24.

Example 18 – Person with joint control



Mrs X has an investment in A and B.

For A's financial statements, if Mrs X controls or jointly controls A, B is related to A if Mrs X has control, joint control or significant influence over B.

For B's financial statements, if Mrs X controls or jointly controls B, A is related to B if Mrs X has control, joint control or significant influence over A.

If Mrs X has significant influence (but not control or joint control) over A and B, then A and B are not related to each other.

Example 19 – Close members of the family holding investments



Mr X is the spouse of Mrs X. Mr X has an investment in A and Mrs X has an investment in B.

For A's financial statements, if Mr X controls or jointly controls A, B is related to A if Mrs X has control, joint control or significant influence over B.

For B's financial statements, if Mr X controls or jointly controls B, A is related to B if Mrs X has control, joint control or significant influence over A.

If Mr X has significant influence (but not control or joint control) over A and Mrs X has significant influence (but not control or joint control) over B, A and B are not related to each other.

9.7.3 Related party disclosures for joint ventures

IAS 24 includes several relationships involving joint ventures in its definition of related party transactions. IAS 24 only refers to joint ventures, and not joint operations.

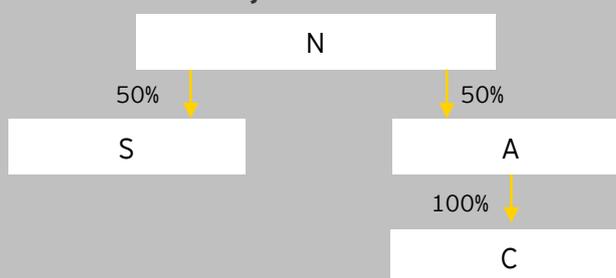
The requirement to disclose related party transactions related to joint ventures also applies to investments held by venture capital organisations, even when the investment is accounted for at fair value, rather than under the equity method.

IAS 24 states, with respect to joint ventures, that an entity is related to a reporting entity if:

- ▶ One entity is a joint venture of the other entity (or an associate or joint venture of a member of a group of which the other entity is a member). Therefore, any joint venturer and its joint venture are related parties.
- ▶ Both entities are joint ventures of the same third party (including subsidiaries of the joint venture). Therefore, a joint venture's subsidiary and the joint venturer are related to each other. This is illustrated in Example 20.
- ▶ One entity is a joint venture of a third entity and another entity is an associate of the third entity. Therefore, an associate and a joint venture are related parties when they share the same investor/joint venturer. This is illustrated in Example 21.

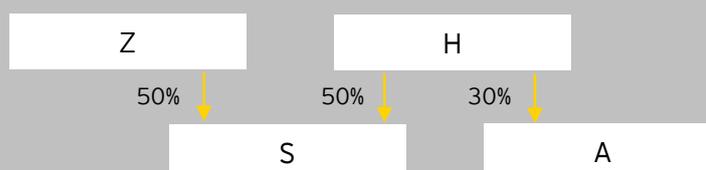
The entity is controlled or jointly controlled by a person identified in Section 9.7.2, or a close member of that person's family, who has control or joint control over the reporting entity. This is illustrated in Examples 20 and 21.

Example 20 – Entities that are joint ventures of the same third party



S and A are joint ventures of N and are, therefore, related parties. C, as a subsidiary of A, is also a related party of N and S.

Example 21 – Entities that are joint ventures and associates of the same third entity



S is a joint venture of H and A is an associate of H. Therefore, S and A are related parties. However, Z and H are not related parties, as discussed in Section 9.7.5.

9.7.4 Government-related entities

IAS 24 uses the concept of government-related entities, which are entities that are controlled, jointly controlled or significantly influenced by a government.

'Government' in this context refers to government, government agencies and similar bodies whether local, national or international. There may be diversity in practice across different jurisdictions in defining what is meant by government.

When an entity is controlled, jointly controlled or significantly influenced by a government, relationships, transactions and outstanding balances, including commitments with that government are related party transactions under IAS 24. Similarly, transactions and outstanding balances, including commitments, with other entities controlled, jointly controlled or significantly influenced by that government are classified as related party transactions under IAS 24. Related party transactions with government-related entities are exempted from certain disclosure requirements. This is discussed in further detail in Chapter 35 of *International GAAP*® 2014.

9.7.5 Parties that are not related parties

IAS 24 clarifies that the following are not related parties:

- ▶ Two entities that have a director or other member of key management personnel in common or because a member of key management personnel of one entity has significant influence over the other entity
- ▶ Two joint venturers that share joint control of a joint venture
- ▶ Providers of finance, trade unions, public utilities and departments and agencies of a government that does not control, jointly control or significantly influence the reporting entity, simply by virtue of their normal dealings with the entity (even though they may affect the freedom of action of an entity or participate in its decision-making process)
- ▶ A customer, supplier, franchisor, distributor or general agent with whom an entity transacts a significant volume of business, simply by virtue of the resulting economic dependence

The reason for these exclusions is that, without them, many entities that are not normally regarded as related parties could fall within the definition of related party.

Appendix – Defined terms

Control	An investor controls an investee when the investor is exposed, or has rights, to variable returns from its involvement with the investee and has the ability to affect those returns through its power over the investee.
Joint arrangement	An arrangement of which two or more parties have joint control.
Joint control	The contractually agreed sharing of control of an arrangement, which exists only when decisions about the relevant activities require the unanimous consent of the parties sharing control.
Joint operation	A joint arrangement whereby the parties that have joint control of the arrangement have rights to the assets, and obligations for the liabilities, relating to the arrangement.
Joint operator	A party to a joint operation that has joint control of that joint operation.
Joint venture	A joint arrangement whereby the parties that have joint control of the arrangement have rights to the net assets of the arrangement.
Joint venturer	A party to a joint venture that has joint control of that joint venture.
Party to a joint arrangement	An entity that participates in a joint arrangement, regardless of whether that entity has joint control of the arrangement.
Power	Existing rights that give the current ability to direct the relevant activities.
Protective rights	Rights designed to protect the interest of the party holding those rights without giving that party power over the entity to which those rights relate.
Relevant activities	Activities of the investee that significantly affect the investee's returns.
Separate vehicle	A separately identifiable financial structure, including separate legal entities or entities recognised by statute, regardless of whether those entities have a legal personality.

About EY

EY is a global leader in assurance, tax, transaction and advisory services. The insights and quality services we deliver help build trust and confidence in the capital markets and in economies the world over. We develop outstanding leaders who team to deliver on our promises to all of our stakeholders. In so doing, we play a critical role in building a better working world for our people, for our clients and for our communities.

EY refers to the global organization, and may refer to one or more, of the member firms of Ernst & Young Global Limited, each of which is a separate legal entity. Ernst & Young Global Limited, a UK company limited by guarantee, does not provide services to clients. For more information about our organization, please visit ey.com.

About EY's International Financial Reporting Standards Group

A global set of accounting standards provides the global economy with one measure to assess and compare the performance of companies. For companies applying or transitioning to International Financial Reporting Standards (IFRS), authoritative and timely guidance is essential as the standards continue to change. The impact stretches beyond accounting and reporting, to key business decisions you make. We have developed extensive global resources – people and knowledge – to support our clients applying IFRS and to help our client teams. Because we understand that you need a tailored service as much as consistent methodologies, we work to give you the benefit of our deep subject matter knowledge, our broad sector experience and the latest insights from our work worldwide.

© 2014 EYGM Limited.
All Rights Reserved.

EYG No. AU2512

ED None



In line with EY's commitment to minimize its impact on the environment, this document has been printed on paper with a high recycled content.

This material has been prepared for general informational purposes only and is not intended to be relied upon as accounting, tax, or other professional advice. Please refer to your advisors for specific advice.

ey.com