The views expressed in this presentation are those of the presenter, not necessarily those of the IASB or IFRS Foundation.
Overview

1. Consolidated financial statements and the link to the Conceptual Framework

2. Why the IASB issued IFRS 10

3. IFRS 10: Main features

4. Conclusion
   1. IFRS 10 summarised
   2. Interaction between IFRSs 9-10-11-12 and IAS 28
Objective: information that is useful to users in making decisions about providing resources to the entity.

Decision-making requires assessment of entity’s prospects for future net cash inflows.

Information about resources of the entity, claims against the entity, and how efficiently and effectively is the use the entity’s resources.

Core principle of IFRS 10: reporting entity presents consolidated financial information (i.e., including information about controlled entities).
## Why the IASB issued IFRS 10

<table>
<thead>
<tr>
<th>Issues – IAS 27 / SIC12</th>
<th>Solution – IFRS 10, 12</th>
</tr>
</thead>
</table>
| **Inconsistencies in practice**  
  - Tension between IAS 27 (control) and SIC 12 (risk and rewards) |  
  - A single control model for all entities  
  - Clear principle of control  
  - Additional application guidance |
| **Disclosures and financial crisis**  
  - Sufficient guidance for structured entities?  
  - Reputational risk as a basis for consolidation?  
  - Inadequate disclosures? |  
  - SIC 12 performed well. Use of existing principles to create a sound foundation for SPEs  
  - Enhanced disclosures particularly for unconsolidated structured entities |
IFRS 10: Main features
IFRS 10: Scope for a single consolidation model

**PRIMARY USERS OF FINANCIAL INFORMATION**
- Investors
- Lenders
- Other creditors

**ECONOMIC ENTITY**
- ENTITY A (Parent-Investor)
- ENTITY B (Subsidiary)
- ENTITY C (Subsidiary)

**GROUP**
- Consolidated financial statements (A+B+C)

**CONTROL**
- CONTROL

**Investment in D** is an asset in A’s statement of financial position.

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Definition of 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.
IFRS 10: Main features

• “De facto” control
  • Entity can control with less than 50% of voting rights
  • Consider:
    • Size of the holding relative to the size and dispersion of other vote holders
    • Potential voting rights
    • Other contractual rights
    • Additional “facts and circumstances” that provide evidence of power (e.g. voting patterns at previous board meetings)

• Structured entities
  • Apply general principles
IFRS 10: Main decisions

• Potential voting rights (PVR)
  • Substantive PVR can give the holder power
  • Consider terms and conditions, including:
    • Barriers preventing holder from exercising
    • Whether exercise of rights would be beneficial to the holder
    • If rights are exercisable when decisions need to be made

• Agency relationships
  • Consider:
    • Scope of decision-making authority
    • Rights held by other parties (e.g., kick-out rights)
    • Remuneration of decision-maker
    • Other interests held by decision-maker in the investee
IFRS 10: General principles in assessing control of an investee

- Consider the purpose and design
- Identify the activities of the investee that significantly affect the returns of the investee (relevant activities)
- Identify how decisions about relevant activities are made
- Determine whether the rights of the investor give it the ability to direct the relevant activities (see next slide)
- Determine whether the investor is exposed, or has rights, to the variability associated with the returns of the investee
- Determine whether the investor has the ability to use its power over the investee to affect its own returns
Example: Assessing Power

- Entity A and B each have 50% ownership interest in the trust.
- Entity A appointed as manager of trust.
- Manager: manages the assets of the trust, approves sellers permitted to sell to the trust, makes decisions about funding of the trust. Cannot be removed without cause.
- Relevant activities?
- Who directs?
Example: Control <50% voting rights

- Investor A owns 40% of voting rights and, via shareholding, has appointed the Chairman and CEO of Investee.
- Does Investor A control Investee?
  - If the other investors are widely dispersed (there are thousands of other investors)?
  - If there are only two other investors?
  - If other investors holding 40% actively participate in shareholders meetings?
- What if Investor A sells 10% of its shareholding?
Example: Structured entities

- Investor A transfers receivables to securitisation vehicle and appoints Servicer B to manage day-to-day cash flow streams
- Investor A can step in and manage the receivables upon default
- Investor A holds notes issued by Securitisation vehicle
- Does Investor A control Securitisation vehicle?
Example: Agency relationships

- Decision-maker A has broad decision making powers
- Can be removed by simple majority vote of investors
- Remunerated via market-based fee – 1% of assets under management and 20% of profits over a hurdle
- Does Decision-maker A control Investment trust if it has:
  - no equity interest?
  - equity interest of 2%?
  - equity interest of 20%?
Example: Delegated rights

Responsible Entity:
- Broad decision making powers
- Removal by simple majority
- Remunerated via market-based fee - 1% of assets under management and 20% of profits over a hurdle
- Equity interest of 20%
Exception to the principle that ALL subsidiaries shall be consolidated: Published October 2012

Investment entity?

- Obtains funds (one or more investors) for providing investment management services
- Business purpose: invest funds solely for returns from investment income and/or capital appreciation
- Measures and evaluates performance of investments on a fair value basis

Accounting …
Accounting

• Measure **ALL** investments in subsidiaries at fair value through profit and loss (IFRS 9 *Financial Instruments*) except...
  – subsidiary that provides services that relate to the investment entity’s investment activities

• **Parent of an investment entity** (*that is not an investment entity*): consolidates **ALL** controlled subsidiaries *including* the ones *controlled through* an investment entity subsidiary
Example: Investment Entities

• Limited Partnership: formed in 20X1 with a 10-year life.
• Offering memo states purpose as to invest in entities with rapid growth potential with the objective of realising capital appreciation.
• Entity GP=1% of capital; 75 partners (unrelated to GP)=remaining 99% of capital.
• 20X1 → no investment; 20X2 → one controlling interest; 20X3 → investment in five additional companies.
• No other activities other than investing.
• Measures and evaluates investments in FV basis.
• Plan to dispose of interests.
Conclusion
IFRS 10: The control model summarised

 ✓ Consolidation: based on control – ‘power so as to benefit’
   ▪ Controller *exposed* to risks and rewards.
   ▪ Exposure: indicator of control but is *not control of itself*
   ▪ *Power* arising from voting rights

 ✓ *Single consolidation model* applied to all entities, including structured entities
Interaction: IFRSs 9, 10, 11 & 12 and IAS 28

Control alone?
- yes
  - Consolidation in accordance with IFRS 10
    - Disclosures in accordance with IFRS 12
- no
  - Joint control?
    - yes
      - Define type of joint arrangement in accordance with IFRS 11
        - Joint Operation
          - Account for assets, liabilities, revenues and expenses
          - Disclosures in accordance with IFRS 12
        - Joint Venture
          - Account for an investment in accordance with IAS 28
          - Disclosures in accordance with IFRS 12
    - no
      - Significant influence?
        - yes
          - IFRS 9
        - no
Thank you (agomes@ifrs.org)
Executive IFRS Workshop for Regulators – Vienna

IFRS 11 Joint Arrangements including related disclosures in IFRS 12

Mariela Isern
Senior Technical Manager, IASB

The views expressed in this presentation are those of the presenter, not necessarily those of the IASB or IFRS Foundation.
Overview

IFRS 11: assessing its population

- overview of joint venture activity 1990–2010; and
- joint venture structures

IFRS 11: assessing its financial statements’ effects

Feedback received from the banking industry

Why IFRS 11? Main features of the Standard

IFRS 12 *Disclosure of Interests in Other Entities*
IFRS 11: assessing its population
IFRS 11: the new IFRS on Joint Arrangements

- IFRS 11 forms part of a package of five Standards (IFRS 10, IFRS 11, IFRS 12, IAS 27 and IAS 28) published in May 2011.
- It replaces IAS 31 *Interest in Joint Ventures* and SIC-13 *Jointly Controlled Entities—Non-Monetary Contributions by Venturers*.
- The disclosure requirements for parties to a joint arrangement are specified in IFRS 12.
- These Standards are to be applied for annual periods beginning on or after 1 January 2013. Earlier application is permitted.
Joint venture activity: frequency, countries, industries

In accordance with IFRS 11:

- **Joint arrangement** is an arrangement in which two or more parties have joint control.
- **Joint control** is the contractually agreed sharing of control, which exists only when decisions about the relevant activities of an arrangement require the unanimous consent of the parties sharing control.

### JV deals by country (1990-2010)

<table>
<thead>
<tr>
<th>Country</th>
<th>JV deals</th>
<th>Relevance</th>
</tr>
</thead>
<tbody>
<tr>
<td>United States</td>
<td>31,952</td>
<td>37.10%</td>
</tr>
<tr>
<td>China</td>
<td>6,078</td>
<td>7.05%</td>
</tr>
<tr>
<td>Japan</td>
<td>4,840</td>
<td>5.62%</td>
</tr>
<tr>
<td>United Kingdom</td>
<td>3,112</td>
<td>3.61%</td>
</tr>
<tr>
<td>Canada</td>
<td>2,610</td>
<td>3.03%</td>
</tr>
<tr>
<td>Australia</td>
<td>2,477</td>
<td>2.88%</td>
</tr>
<tr>
<td>India</td>
<td>2,093</td>
<td>2.43%</td>
</tr>
<tr>
<td>Germany</td>
<td>1,541</td>
<td>1.79%</td>
</tr>
<tr>
<td>Malaysia</td>
<td>1,303</td>
<td>1.51%</td>
</tr>
<tr>
<td>Russian Federation</td>
<td>914</td>
<td>1.06%</td>
</tr>
<tr>
<td>Others</td>
<td>29,215</td>
<td>33.92%</td>
</tr>
<tr>
<td><strong>Total number of JV deals</strong></td>
<td><strong>86,135</strong></td>
<td><strong>100.00%</strong></td>
</tr>
</tbody>
</table>

### JV deals by industry (1990-2010)

<table>
<thead>
<tr>
<th>Industry</th>
<th>JV deals</th>
<th>Relevance</th>
</tr>
</thead>
<tbody>
<tr>
<td>Business services</td>
<td>17,610</td>
<td>20.45%</td>
</tr>
<tr>
<td>Software</td>
<td>6,718</td>
<td>7.80%</td>
</tr>
<tr>
<td>Wholesale trade: durable goods</td>
<td>5,840</td>
<td>6.78%</td>
</tr>
<tr>
<td>Investment and commodity firms</td>
<td>4,980</td>
<td>5.78%</td>
</tr>
<tr>
<td>Electronic</td>
<td>3,321</td>
<td>3.86%</td>
</tr>
<tr>
<td>Telecommunications</td>
<td>2,545</td>
<td>2.95%</td>
</tr>
<tr>
<td>Wholesale trade: non-durable goods</td>
<td>2,300</td>
<td>2.67%</td>
</tr>
<tr>
<td>Mining</td>
<td>2,297</td>
<td>2.67%</td>
</tr>
<tr>
<td>Oil and gas</td>
<td>2,166</td>
<td>2.51%</td>
</tr>
<tr>
<td>Real estate</td>
<td>1,781</td>
<td>2.07%</td>
</tr>
<tr>
<td>Others</td>
<td>36,577</td>
<td>42.46%</td>
</tr>
<tr>
<td><strong>Total number of JV deals</strong></td>
<td><strong>86,135</strong></td>
<td><strong>100.00%</strong></td>
</tr>
</tbody>
</table>

In accordance with IFRS 11:

- **Joint arrangement** is an arrangement in which two or more parties have joint control.
- **Joint control** is the contractually agreed sharing of control, which exists only when decisions about the relevant activities of an arrangement require the unanimous consent of the parties sharing control.


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Joint venture activity: structures

JV deals by form (1990-2010)

<table>
<thead>
<tr>
<th></th>
<th>Strategic alliances</th>
<th>Independent firms</th>
<th>Total</th>
</tr>
</thead>
<tbody>
<tr>
<td>Total number of JV deals</td>
<td>54,567</td>
<td>31,568</td>
<td>86,135</td>
</tr>
<tr>
<td>Relative relevance</td>
<td>63.4%</td>
<td>36.6%</td>
<td>100.0%</td>
</tr>
</tbody>
</table>

JV Deals by country and form - 1990-2010

JV Deals by industry and form - 1990-2010

IFRS 11: assessing its effects
From IAS 31 to IFRS 11

Joint ventures: joint control

**Jointly controlled operations**
Recognition of assets, liabilities, revenues and expenses

**Jointly controlled assets**
Recognition of assets, liabilities, revenues and expenses

**Jointly controlled entities**
Proportionate consolidation or equity method

Jointly controlled entities:

**Jointly controlled entities**
Proportionate consolidation or equity method

Joint operations:
Recognition of assets, liabilities, revenues and expenses

Joint ventures:
Equity method

Joint arrangements: joint control

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Accounting methods pre-IFRS 11

Financial statement effects: overview of the effects

Population of JV deals

37% (1)

Independent firms

50% (2)

Proportionate consolidation

Joint operation

Joint venture

No changes due to IFRS 11

IFRS 11 will cause changes in the accounting

63% (1)

Strategic alliances

50% (2)

Equity method

Joint operation

Joint venture

No changes due to IFRS 11

No changes due to IFRS 11

(1) Source: Thomson Financial SDC Platinum Alliance/Joint Ventures database covering joint venture deals established during 1990-2010

(2) Source: KPMG HRG Limited and Dr Isabel von Keitz. The Application of IFRS Choices in Practice – December 2006
## Changes in the financial statements

<table>
<thead>
<tr>
<th>Financial statements</th>
<th>Effects due to the accounting change*</th>
</tr>
</thead>
</table>
| Statement of financial position       | • Reported figures will decline (ie total assets and total liabilities will decrease).  
• The investment in the joint venture will be captured in a single line item. |
| Statement of comprehensive income    | • Reported figures will decline (ie total revenues and total expenses will decrease).  
• No changes in net income. |
| Statement of changes in equity        | • No changes in the statement of changes in equity. |
| Statement of cash flows               | • Reported operating, investing and financing cash flow figures will decline.  
• Dividends received from joint ventures will be presented as cash flows. |

(*) This is considering those arrangements that were accounted for using proportionate consolidation that will be accounted for using the equity method.
### Changes in key ratios

<table>
<thead>
<tr>
<th>Ratios</th>
<th>Effects due to the accounting change*</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Return on capital</strong></td>
<td>- The accounting change will not affect this ratio.</td>
</tr>
<tr>
<td>(for example, net income/shareholders’ equity)</td>
<td></td>
</tr>
<tr>
<td><strong>Profitability</strong></td>
<td>- The removal of the proportionate share of revenue will cause profitability to increase.</td>
</tr>
<tr>
<td>(for example, net income/revenue)</td>
<td></td>
</tr>
<tr>
<td><strong>Total assets turnover</strong></td>
<td>- The accounting change will cause the reported revenue and the total asset to be smaller. The final effect on this ratio will depend upon the absolute and relative changes of revenues and assets.</td>
</tr>
<tr>
<td>(for example, revenue/assets)</td>
<td></td>
</tr>
<tr>
<td><strong>Financial leverage</strong></td>
<td>- The removal of the entities’ proportionate share of debt will cause the leverage ratio to be smaller.</td>
</tr>
<tr>
<td>(for example, net debt/capital employed, debt/shareholders’ equity)</td>
<td></td>
</tr>
</tbody>
</table>

(*): This is considering those arrangements that were accounted for using proportionate consolidation that will be accounted for using the equity method.
Feedback from the banking industry
Feedback received from regulators when IFRS 11 was being developed

- Frequency and significance of joint arrangements appeared to be limited to a relatively small number of institutions.

- Impact on capital requirements expected to be little.

- In favour of maintaining proportional consolidation because of the following:

  (i) it provides greater transparency for institutions, investors and supervisors because it provides more information in the financial statements; and

  (ii) an entity is put in a position where it could increase its risk-taking potential because asset figures are a key determinant of regulated firms’ capital requirements.
Respondents to Exposure Draft 9 *Joint Arrangements (ED9)* from the banking industry

<table>
<thead>
<tr>
<th>Industry</th>
<th>Number of respondents to ED 9</th>
<th>Respondents that use proportionate consolidation</th>
<th>Jointly controlled entities’ assets/consolidated assets</th>
<th>Jointly controlled entities’ revenues/consolidated revenues</th>
<th>Profitability increase as a result of eliminating proportionate consolidation (basis points)**</th>
</tr>
</thead>
<tbody>
<tr>
<td>Banking*</td>
<td>9</td>
<td>3</td>
<td>3.9%</td>
<td>14.3%</td>
<td>98</td>
</tr>
<tr>
<td>TOTAL RESPONDENTS</td>
<td>111</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

(*): Only one of the three respondents using proportionate consolidation prepared consolidated financial statements with enough information to perform the analysis shown in this table.

(**): Profitability is measured by the basis points increase in the net income to revenues ratio.

Main feedback received on ED 9 from banking industry respondents:

- new concepts were not presented sufficiently clear in the Exposure Draft;
- further clarification on the classification of the different types of arrangements was deemed necessary; and
- generally, no support or reservations about the removal of proportionate consolidation.
Why IFRS 11?
Frameworks with different objectives

“We have to accept that the regulatory framework and accounting framework have different objectives. One is to serve the public interest in terms of transparency and picturing economic transactions, and the other is the safety and soundness of banks.”

Senior International Banking Regulator, Risk Magazine, 29 April 2013
IAS 31: what needed to be improved

The structure of the arrangement is the only driver for the accounting.

When arrangements are structured in entities, preparers have an accounting option.

- Jointly controlled operations
- Jointly controlled assets
- Jointly controlled entities
- Accounting for assets, liabilities, revenues and expenses in accordance with the contractual arrangements
- Proportionate consolidation
- Equity method

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The principle in IFRS 11

IFRS 11 establishes a principle-based approach for the accounting for joint arrangements

Parties to a joint arrangement recognise their rights and obligations arising from the arrangement
IFRS 11: the required assessments

1st assessment

JOINT CONTROL

Do all of the parties, or a group of the parties, have joint control of the arrangement?

No

Outside the scope of IFRS 11

Yes

Classification of the JOINT ARRANGEMENT

Analysis of the parties’ rights and obligations arising from the arrangement

Joint Operation

Joint Venture

2nd assessment
Assess the parties’ rights and obligations arising from the arrangement by considering:

(a) the legal form of the separate vehicle;
(b) the terms of the contractual arrangement; and, if relevant
(c) other facts and circumstances.

Parties have rights to the assets and obligations for the liabilities

Joint venture

Accounting for an investment using the equity method

Parties have rights to the net assets

Joint operation

Accounting for assets, liabilities, revenues and expenses in accordance with the contractual arrangements

Assessment of the parties’ rights and obligations

Accounting reflects the parties’ rights and obligations

Not structured through a separate vehicle* 

Structured through a separate vehicle*

(*): A separate vehicle is a separately identifiable financial structure, including separate legal entities or entities recognised by statute, regardless of whether those entities have a legal personality.
Structured in separate vehicles

Legal form of the separate vehicle

Does the legal form of the separate vehicle give the parties rights to the assets, and obligations for the liabilities, relating to the arrangement?

Yes

Terms of the contractual arrangement

Do the terms of the contractual arrangement specify that the parties have rights to the assets, and obligations for the liabilities, relating to the arrangement?

Yes

No

Other facts and circumstances

Have the parties designed the arrangement so that (a) its activities primarily aim to provide the parties with an output (i.e., the parties have rights to substantially all of the economic benefits of the assets held in the separate vehicle); and (b) it depends on the parties on a continuous basis for settling the liabilities relating to the activity conducted through the arrangement?

Yes

No

Joint Venture

Joint Operation
**Example**—contractual terms reverse the legal features of the separate vehicle

- A and B (the parties) set up a separate vehicle (entity H) and a joint operating agreement (JOA) to undertake oil and gas exploration, development and production activities.

- The main feature of entity H’s legal form is that it causes the separate vehicle to be considered in its own right.

- The JOA specifies that the rights and obligations arising from the exploration, development and production activities shall be shared between the parties (ie the permits, the production obtained, all costs associated with the activities, taxes payable etc).
Example—other facts and circumstances

- Two parties structure a joint arrangement in an incorporated entity (entity C) in which each party has a 50 per cent ownership interest. The purpose of the arrangement is to manufacture materials required by the parties for their own individual manufacturing processes.

- The legal form of entity C (an incorporated entity) through which the activities are conducted initially indicates that the assets and liabilities held in entity C are the assets and liabilities of entity C.

- The contractual arrangement between the parties does not specify that the parties have rights to the assets or obligations for the liabilities of entity C.
The parties are each obliged to purchase half of the output produced by entity C. Entity C cannot sell any of the output to third parties, unless this is approved by the two parties to the arrangement. Because the purpose of the arrangement is to provide the parties with output that they require, such sales to third parties are expected to be uncommon and not material.

The price of the output is set at a level that is designed to cover the costs of production and administrative expenses incurred by entity C. On the basis of this operating model, the arrangement is intended to operate at a break-even level.
Improvements

Enhanced *verifiability* and *understandability*

- the accounting more faithfully reflects the economic phenomena that it purports to represent.

Improved *consistency*

- it provides the same accounting outcome for each type of joint arrangement.

More *comparability* among financial statements

- it will enable users to identify and understand similarities in, and differences between, different arrangements.
IFRS 12
Scope

Combined disclosure standard for:

- subsidiaries;
- joint arrangements;
- associates; and
- unconsolidated structured entities.
Disclosure objective

To disclose information that helps users of financial statements evaluate:

(a) the nature of, and risks associated with, an entity’s interests in other entities; and

(b) the financial effects of those interests on the entity’s financial position, financial performance and cash flows.
Joint arrangements and associates

Nature, extent and financial effects of interests in joint arrangements and associates, for example

- list and nature of interests in individually-material joint arrangements and associates.
- detailed quantitative summarised financial information for each individually-material joint venture and associate, and in total for all others.
- fair value of investments in individually-material JVs and associates (if published quoted prices available).
- unrecognised share of losses of joint ventures and associates.
- nature and extent of any significant restrictions on transferring funds.

Nature of, and changes in, the risks associated with the involvement

- commitments and contingent liabilities.
Quantitative summarised financial information for individually-material joint ventures

- Dividends received from the joint venture.

- Summarised financial information including, but not limited to:
  - cash and cash equivalents included in current assets;
  - current assets;
  - non-current assets;
  - current liabilities;
  - current financial liabilities included in current liabilities;
  - non-current liabilities;
  - non-current financial liabilities included in non-current liabilities;
  - revenue;
  - depreciation and amortisation;
  - interest income;
  - interest expense;
  - profit or loss from continuing operations;
  - income tax expense or income;
  - post-tax profit or loss from discontinued operations;
  - other comprehensive income; and
  - total comprehensive income.

Underline indicates new disclosure