IFRS 11 Joint Arrangements IAS 28 Investments in Associates and Joint Ventures

Noora Hakkarainen

Manager, EY

Building a better working world

Noora Hakkarainen

Manager, EY, Financial Accounting Advisory Services

noora.hakkarainen@fi.ey.com

Work experience

Manager, Financial Accounting Advisory Services, 2016 – present

Examples of professional experience:

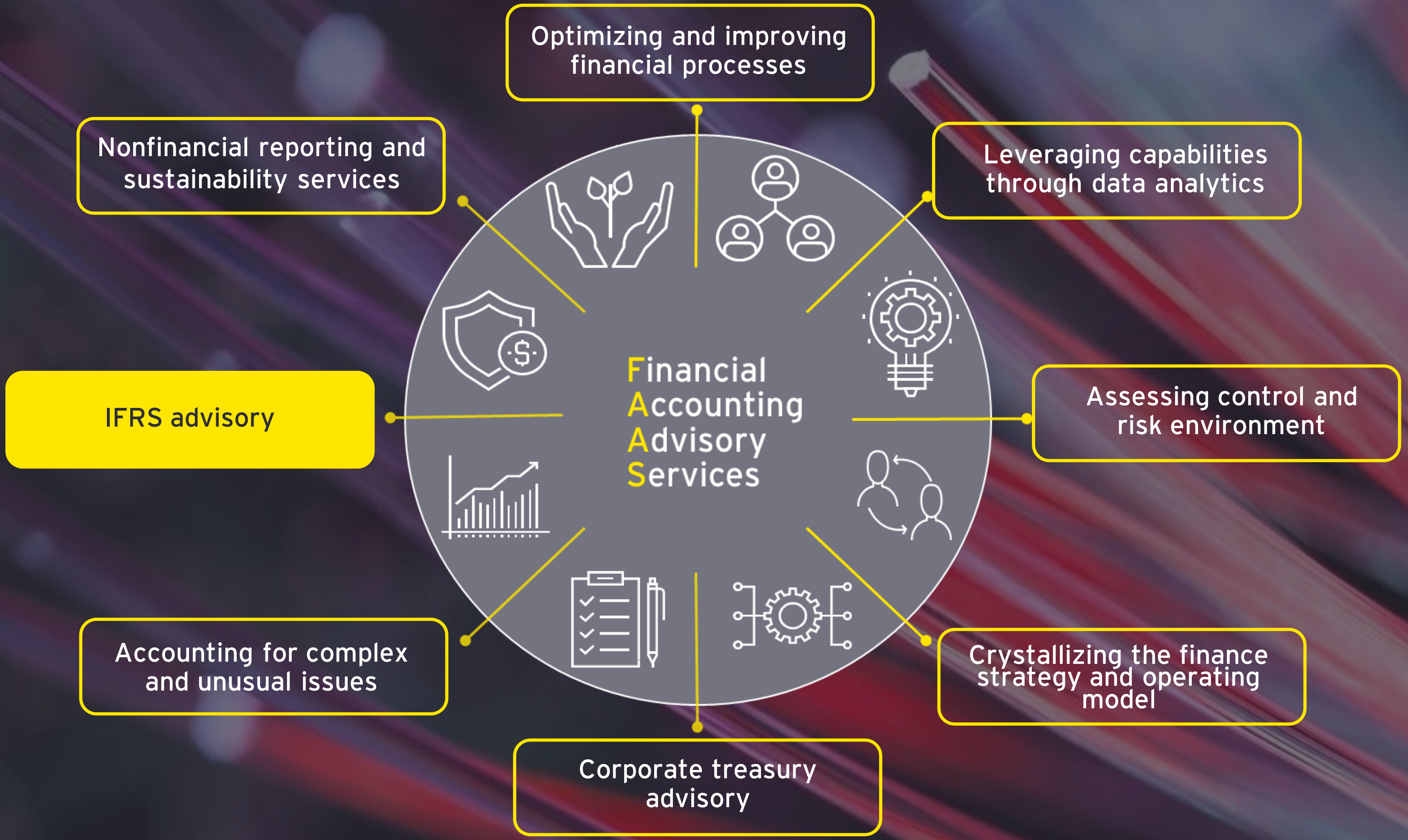
- Leading projects with hands-on involvement to implement IFRS 16 Leases and IFRS 15 Revenue from Contracts with Customer in Finnish publicly listed companies.
- Leading IFRS Conversion projects from Finnish GAAP to IFRS in Finnish private equity owned companies planning an IPO.
- Leading a process and internal controls development project in a Finnish publicly listed company.

Education

University of Vaasa

Graduated in 2015 with Master's in Accounting and Auditing

EY Financial Accounting Advisory Services (FAAS) team - Core services



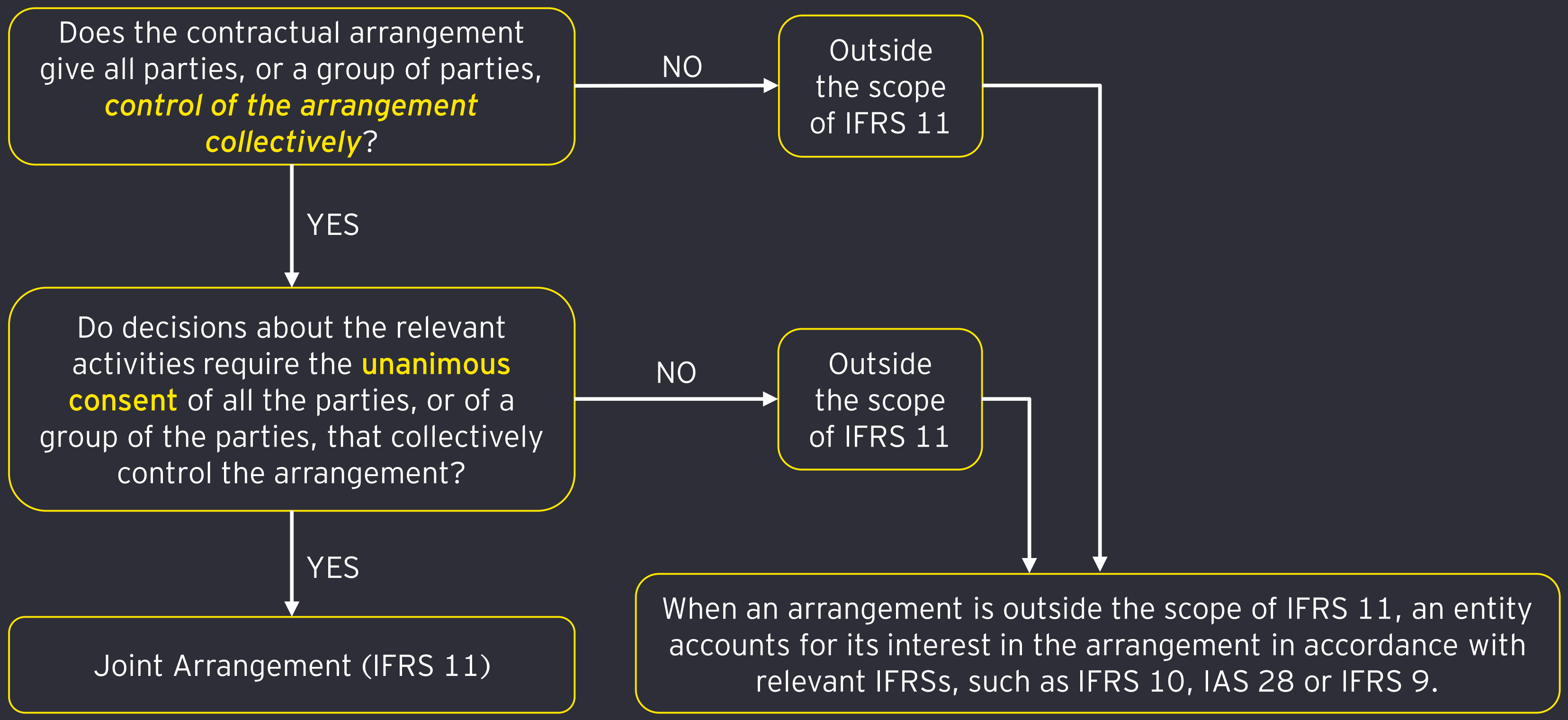
Overview: Standards for consolidation

	IFRS 10	IFRS 11	IAS 28	IFRS 9
	Subsidiary	Joint Arrangement	Associate	Other investment
Subsidiary	Control	Joint control	Significant influence	No control or significant influence
"Share"	> 50%	Equal	> 20%	< 20%
Accounting	Consolidation	In relation to investor's interest in the arrangement	Equity method	Fair value

IFRS 11 - Joint Arrangements: Joint control

A "joint arrangement" exists if two or more parties exercise joint control over an entity. In a joint control arrangement decisions about relevant activities require unanimous consent of the parties sharing control.

Assessing joint control (IFRS 11)



Case – Joint control

- Company A, B and C have established a Joint Venture by signing a Shareholders' Agreement. The Agreement specifies that at least 75 per cent of the voting rights are required to make decisions about the relevant activities of the arrangement. In the Agreement the voting rights of the parties are as follows:
  - A has 50% of the voting rights
  - B has 30% of the voting rights
  - C has 20% of the voting rights

Is this a joint control arrangement?

Since the terms of the Shareholders' Agreement require at least 75 per cent of the voting rights to make decisions about the relevant activities, this implies that A and B have joint control of the arrangement because decisions about the relevant activities of the arrangement cannot be made without both A and B agreeing. (IFRS 11 Joint Arrangements – Application example 1)

What would be the outcome in case entities B and C both have 25% of the voting rights?

A does not control the arrangement because it needs the agreement of either B or C and, thus, A, B and C collectively control the arrangement. However, there is more than one combination of parties that can agree to reach 75 per cent of the voting rights (ie either A and B or A and C). In such a situation, to be a joint arrangement the contractual arrangement between the parties would need to specify which combination of the parties is required to agree unanimously to make decisions about the relevant activities of the arrangement. (IFRS 11 Joint Arrangements – Application example 2)

IFRS 11 - Joint Arrangements: Classification of a Joint Arrangement

Classification of a joint arrangement: assessment of the parties' rights and obligations arising from the arrangement

Structure of the arrangement

- Not structured through a separate vehicle → Joint operation
- Structured through a separate vehicle* →
  An entity shall consider:
  i. The legal form of the separate vehicle;
  ii. The terms of the contractual arrangement; and
  iii. When relevant, other facts and circumstances.
  → Joint operation / Joint venture

Joint operation =

rights to the assets, and obligations for the liabilities, relating to the arrangement

Joint venture =

rights to the net assets of the arrangement

* Separate vehicle = Separately identifiable financial structure, e.g. company or other structure

IFRS 11 - Joint Arrangements: Accounting

Structure of the Joint Arrangement

Joint Venture	Joint Operation
Apply **Equity Method***	**Investor recognises in relation to its interest in a joint operation:**

* IAS 28 Investments in Associates and Joint Ventures

- ✓ Its assets, including it 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 the revenue from the sale of the output by the joint operation
- ✓ Its expenses, including its share of any expenses incurred jointly

IAS 28 - Investments in Associates and Joint Ventures

Objective

- The objective of this Standard is to prescribe the accounting for investments in associates and to set out the requirements for the application of the equity method when accounting for investments in associates and joint ventures.

Scope

- This Standard is applied by all entities that are investors with joint control of, or significant influence over, an investee.

IAS 28 - Investments in Associates and Joint Ventures

Significant influence

> 20%

- If an entity holds, directly or indirectly (e.g. through subsidiaries), 20per cent or more of the voting power of the investee, it is presumed that the entity has significant influence, unless it can be clearly demonstrated that this is not the case.

< 20%

- Conversely, if the entity holds, directly or indirectly (e.g. through subsidiaries), less than 20per cent of the voting power of the investee, it is presumed that the entity does not have significant influence, unless such influence can be clearly demonstrated.

!

- *Analysis is required to determine whether the investor has significant influence over the investee. Sometimes, when the investor holds more than 20% of the voting rights but less than 50%, it can still control the investee.*

IAS 28 - Investments in Associates and Joint Ventures

Significant influence

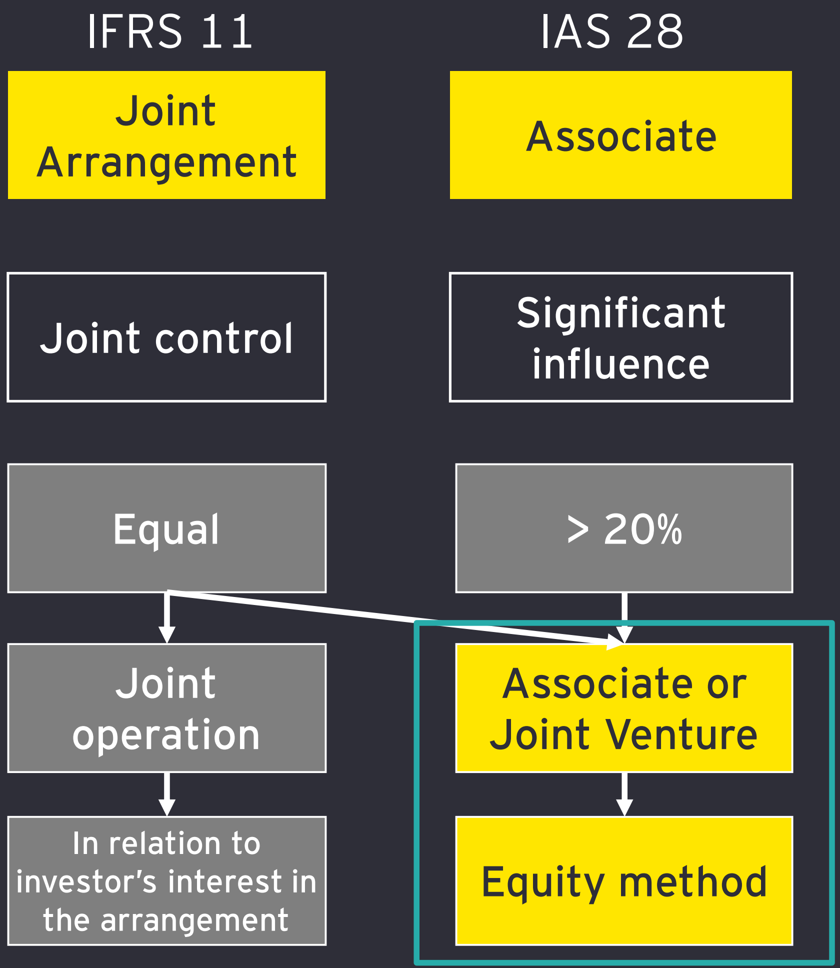
!

The existence of significant influence by an entity is usually evidenced in one or more of the following ways:

- ✓ representation on the board of directors or equivalent governing body of the investee;
- ✓ participation in policy-making processes, including participation in decisions about dividends or other distributions;
- ✓ material transactions between the entity and its investee;
- ✓ interchange of managerial personnel; or
- ✓ provision of essential technical information.

EY

IAS 28 - Investments in Associates and Joint Ventures
Equity method



Initial recognition

- On initial recognition the investment in an associate or a joint venture is recognised **at cost.**

Subsequent recognition

- The carrying amount is increased or decreased to recognise the investor's share of the profit or loss of the investee after the date of acquisition.
- The investor's share of the investee's profit or loss is recognised in the investor's profit or loss.
- Distributions such as dividends received from an investee reduce the carrying amount of the investment.
- Adjustments to the carrying amount may also be necessary for changes in the investor's proportionate interest in the investee arising from changes in the investee's other comprehensive income.

Example: Equity method

Background

- Entity A acquires a 30% interest in Entity B. Entity A has significant influence over Entity B since it holds >20% of the voting rights of Entity B and has representation in the board of directors.
- Cost of the investment is €500.000
- During the first year, B made a profit of €80.000 and paid a dividend of €100.000

Profit during the year

- Share in the profit reported by B (30% of €80.000) recognised as income by A is €24.000
- Dividend received by A during the year (30% of €100.000) is €30.000

Closing balance of A's investment in B in the end of the financial year

Cost of the investment	€500.000
Share of profit recognised as income	+ €24.000
Dividends received	- €30.000
Closing balance of A's investment in B	**€494.000**

Questions?