

## Review of IFRS 11 *Joint Arrangements*

**Objective:** To review IFRS 11 *Joint Arrangements* to consider whether the concerns raised by the AASB in response to IASB ED 9 (AASB ED 157) *Joint Arrangements* have been appropriately addressed and whether there are outstanding issues of concern.

Issues Raised in AASB Submissions	IASB ED 9 Proposals	IASB Approach in IFRS 11
<b>Definitions &amp; terminology</b>		
<p><b>Lack of clarity</b></p> <p>The Board expressed the following concerns:</p> <ul style="list-style-type: none"> <li>▪ there is an insufficient level of detail to enable effective application in practice and may result in inconsistent classification of joint arrangements.</li> <li>▪ there are no specific definitions of: <ul style="list-style-type: none"> <li>- joint operation</li> <li>- joint asset</li> <li>- joint venture</li> </ul> </li> </ul>	<p>ED 9 described the proposed three types of joint arrangement as follows:</p> <p><b>joint operation</b> (para 8): each party uses its own assets, incurs own expenses, liabilities; shared revenue from sale of joint products;</p> <p><b>joint asset</b> (para 11): each party has rights to the asset and takes share of output;</p> <p><b>joint venture</b> (para 15): each party has share of the outcome, but no rights to individual assets or obligations for expenses.</p>	<p>Two types of joint arrangement, defined in the Standard and in Appendix A as follows:</p> <p><b>joint operation:</b> the parties that have joint control have rights to assets, and obligations for liabilities relating to the arrangement – this combines ‘joint operations’ and ‘joint assets’ of the ED, based on common features;</p> <p><b>joint venture:</b> the parties that have joint control have rights to the net assets of the arrangement.</p> <p><u>Staff view</u> – issue resolved – the two types are clearly distinguished.</p>
<p><b>Shared decision-making</b></p> <p>The Board expressed concern that the definition of joint arrangements requires all parties to be involved in shared decision-making. The Board stated that this requirement is too restrictive, will exclude a large number of arrangements from the scope and result in similar interests being treated in different ways.</p> <p>Furthermore, the Board stated that ED 9 does not adequately articulate how the concept is intended to operate and which decisions come under this term. In addition concern was expressed that shared decision-</p>	<p>Definitions proposed in ED 9:</p> <p><b>“joint arrangement:</b> a contractual arrangement whereby two or more parties undertake an economic activity together and share decision-making relating to that activity;</p> <p><b>joint control:</b> the contractually agreed sharing of the power to govern the financial and operating policies of a venture so as to obtain benefits from its activities.”</p>	<p>The definitions have been revised by replacing the terms ‘share decision-making’ and ‘shared decisions’ with the term ‘joint control’, consistent with the term used in the definition of joint ventures.</p> <p>The revised definitions are:</p> <p><b>joint arrangement:</b> an arrangement of which two or more parties have joint control;</p> <p><b>joint control:</b> 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.</p> <p><u>Staff view</u> – issue resolved – all parties no longer required to be involved in decisions; can have mere participants (para 11).</p>

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<p>making is focussed at too low a level to be practically applied and does not reflect commercial reality of most joint arrangements.</p>		
<p><b>Business</b></p> <p>The Board expressed concern that it is unclear whether paragraph 18 of ED 9 merely provides an example of a joint venture or means that a business is required for an entity to have an interest in a joint venture.</p>	<p>Paragraph 18:</p> <p>“A <i>business</i> usually involves assets and resources working together to achieve an outcome, which requires decisions of a financial and operating nature. A business that is subject to <i>joint control</i> is, therefore, a joint venture, unless circumstances indicate otherwise. Such circumstances would indicate that the parties have contractual rights to the assets of the business and have contractual obligations for the expenses of the business.”</p>	<p>Based on feedback, the IASB determined that a ‘business’ as defined in IFRS 3 can be found in all types of joint arrangements and, therefore, the existence of a ‘business’ is not a distinctive feature of a specific type of joint arrangement.</p> <p>The IASB decided that, for a joint arrangement established in a separate entity, it is necessary to take an ‘open assessment’ approach and consider all relevant facts and circumstances to assess whether the arrangement is a joint operation or a joint venture. See para B21: consider legal form of the separate vehicle; contract terms; other facts.</p> <p><u>Staff view</u> – issue resolved – existence of a business not the determinant.</p>
<p><b>Output v Outcome</b></p> <p>The Board expressed concern regarding the ED 9 proposal that parties to a joint venture are entitled to a share of the ‘outcome’ of the activities of the joint venture. The Board questioned whether this meant that an entity with a share of the ‘output’ (product) rather than cash is precluded from treating the investment as a joint venture.</p> <p>The Board felt that this may lead to inconsistent treatment and may also result in the basis of accounting changing from year to year if venturers elect annually to take a share of profit or of output.</p>	<p>Paragraph 15:</p> <p>“A joint venture is a joint arrangement, or part of a joint arrangement, that is jointly controlled by the <i>venturers</i>. The venturers do not have rights to individual assets or obligations for expenses of the venture. Rather, each venturer is entitled to a share of the outcome (eg profit or loss) of the activities of the joint venture.”</p>	<p>The definition of a joint venture does not refer to ‘a share of the outcome’, and therefore is not expressly restricted in the way that concerned the Board. The term ‘outcome’ does not appear in IFRS 11.</p> <p>Paragraph B18 refers to a share of output and revenues. Para B27 (table re revenue) indicates that a joint venture would normally involve the sharing of profits whereas a joint operation could involve either a share of revenue or of profit.</p> <p><u>Staff view</u> – issue resolved – the ability to share output would suggest a joint operation, not a joint venture, whichever election was made. Para 20 requires a joint operator to recognise revenue from share of output and from share of the joint operation’s sales of output.</p>

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<p><b>Current industry terminology</b></p> <p>The Board noted that the ED proposed changing common terminology – ‘joint arrangement’ as the general term instead of ‘joint venture’.</p>	<p>Joint ventures are one type of joint arrangement, alongside joint operations and joint assets. ‘Joint ventures’ to replace the term ‘jointly controlled entities’.</p>	<p>Retained ‘joint arrangement’ as the general term, comprising both joint operations and joint ventures.</p> <p><u>Staff view</u> – issue remains, but not material – we all have to cope with new terms for old things, e.g. outside equity interests, minority interests, non-controlling interests ...</p>
<b>Accounting for joint arrangements</b>		
<p><b>No legal entity for joint venture</b></p> <p>The Board expressed concern that under ED 9 it would be possible for an unincorporated joint arrangement to be classified as a joint venture. The Board was concerned that if correct, this would require equity accounting and would therefore raise the following practical issues:</p> <ul style="list-style-type: none"> <li>▪ how the equity method would be applied when there is no legal entity;</li> <li>▪ how equity movements are determined;</li> <li>▪ what constitutes a dividend;</li> <li>▪ how cost of investment and share of profit/loss would be determined.</li> </ul>	<p>Paragraph 17:</p> <p>“A joint venture often involves the establishment of a legal entity, such as a corporation ...”</p>	<p>Paragraph B16 in the application guidance states that a joint arrangement not structured through a separate vehicle is a joint operation. Under para 20, a joint operation is accounted for in terms of the operator’s assets, liabilities, revenues and expenses.</p> <p>Paragraph B19 states that a joint arrangement structured through a structured vehicle can be either a joint venture or a joint operation. Only an interest in a joint venture is accounted for under the equity method (para 24).</p> <p><u>Staff view</u> – issue resolved – the equity method applies only where there is a separate vehicle for the joint arrangement.</p>
<p><b>Use of the equity method</b></p> <p>The Board expressed concern whether the principle that parties should recognise their contractual rights and obligations would be achieved by requiring the equity method and removing proportionate consolidation. The Board felt the one-line equity method would result in a loss of significantly useful information and the additional disclosures proposed may not compensate for a less transparent accounting method.</p>	<p>The IASB saw the option in IAS 31 of proportionate consolidation or the equity method in accounting for interests in jointly controlled entities as inappropriate.</p> <p>ED 9 proposed the following accounting bases (para’s 21-23):</p> <p><b>joint operation:</b> a party recognises, in accordance with the applicable IFRSs, the assets it controls, liabilities and expenses it incurs, share of revenue and expenses;</p>	<p>The IASB concluded that proportionate consolidation is not an appropriate method to account for interests in joint arrangements when the parties have neither rights to the assets nor obligations for the liabilities relating to the arrangement – hence, interests in joint ventures require the equity method, as the venturer has (only) an interest in the net assets.</p> <p>Furthermore, the IASB concluded that the equity method is not appropriate to recognise interests in joint arrangements when the parties have rights to the assets and obligations for the liabilities relating to the</p>

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<p><b>Enhance faithful representation of joint arrangements in financial statements</b></p> <p>The Board expressed concern that the objective of the ED to enhance faithful representation of joint arrangements would potentially not be satisfied in all cases using the equity method, as it provides little if any useful information for users that reflects the substance of the arrangement. The Board considered that proportionate consolidation provides greater transparency in many cases.</p> <p><b>Justification for removing proportionate consolidation</b></p> <p>The Board argued that the removal of proportionate consolidation for joint ventures had not been justified.</p>	<p><b>joint asset:</b> a party recognises, in accordance with the applicable IFRSs, its share of joint assets and liabilities, revenue from its share of output and liabilities and expenses it incurs;</p> <p><b>joint venture:</b> a venturer accounts for its interest using the equity method of accounting (subject to the usual exceptions: interest is held for sale, entity is a parent exempt from consolidation, or entity is a venturer similar to such a parent).</p>	<p>arrangement – hence, interests in joint operations require the recognition of assets, liabilities, revenues, expenses, including the share of joint elements.</p> <p>The IASB states in paragraph BC44 its belief that accounting for joint arrangements based on the principles of the IFRS will improve faithful representation and enhance comparability. It notes that IFRS 12 requires additional disclosures for material joint ventures that are more detailed than under IAS 31 with proportionate consolidation.</p> <p><u>Staff view</u> – issue resolved – recognition basis reflects the substance of the entity’s interest in arrangement. Additional disclosures per IFRS 12 (para’s B12, B13) of summarised financial information for material joint ventures provide the kind of information the AASB was concerned would be lost under the equity method.</p>
<p><b>Applicable IFRSs</b></p> <p>The Board expressed concern that ED 9 does not provide further guidance on the requirement to recognise assets, liabilities, revenues and expenses in respect of interests in a joint operation or joint asset “in accordance with ‘applicable IFRSs’ ”.</p> <p>The Board queried Illustrative Example 2 and whether a proportionate share of a tangible asset should result in the recognition of an intangible asset.</p>	<p>Refer to the proposed accounting bases in the issue immediately above.</p> <p>Example 2 – Five advertising companies jointly buy a jet aircraft. They enter into an agreement whereby each party has the right to use the aircraft for its own purposes some days each year.</p> <p>The arrangement involves a joint asset. The joint arrangement is a way to share the costs of having access to an aircraft. Each party has a unilateral right to use the jet aircraft for its own purposes some days each year, and would also have rights to its share of any residual value of the aircraft. It is those rights that the parties control and would recognise in accordance with applicable IFRSs.</p>	<p>Paragraph 21: ‘A joint operator shall account for the assets, liabilities, revenues and expenses relating to its interest in a joint operation in accordance with the IFRSs applicable to the particular assets, liabilities, revenues and expenses.’</p> <p>This results in a minor clarification to direct the reader to an IFRS applicable to the specific assets, liability, revenue or expense rather than simply to IFRSs with no further guidance provided.</p> <p><u>Staff view</u> – issue resolved.</p>

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<p><b>Unit of Account</b></p> <p>The Board considered there may be difficulties in practice in applying the unit of account notion whereby parts of assets (e.g. a floor of a building) are recognised as the unit of account. The Board felt this concept may be premature in preceding the IASB’s fundamental research on the conceptual framework.</p> <p>In addition, the Board expressed concern that there appeared to be a conflict with the requirements of IFRIC 4, which takes an all-or-nothing approach under which an asset is not recognised under a lease unless substantially all of the output flows to the entity, even when the entity has unilateral control over the output that does flow.</p>	<p>Paragraph 22:</p> <p>“In respect of its interest in a joint asset, a party shall recognise, in accordance with applicable IFRSs:</p> <p>(a) its share of the joint asset, classified according to the nature of the asset;</p> <p>(b) any liabilities it incurs;</p> <p>(c) its share of any liabilities incurred jointly with the other parties to the joint arrangement;</p> <p>(d) ...”</p>	<p>Paragraph 20 states that a joint operator shall recognise its share of any assets held jointly and its share of any liabilities incurred jointly.</p> <p>In paragraph BC40, the IASB acknowledged the concern raised in regard to how the unit of account relating to the share of assets and liabilities to be accounted for by the parties to a joint operation should be delineated. The IASB noted that it had not intended to change this aspect of IAS 31, where the ‘share’ is determined in accordance with the contractual arrangement.</p> <p><u>Staff view</u> – issue resolved, or at least an existing issue remains – staff also note that Interpretation 4 does not preclude a lease of a portion of a larger asset, but does exclude such from its scope (see para’s 3 and BC9-BC12).</p>
<p><b>Disclosures</b></p>		
<p><b>Proposed additional and reinstated disclosures</b></p> <p>The Board’s comments on the disclosures proposed in ED 9 are addressed in the review of IFRS 12 <i>Disclosure of Interests in Other Entities</i> (see agenda paper 8.4.1).</p>		
<p><b>Other accounting issues (7 May 2010 submission)</b></p>		
<p><b>Contributions of non-monetary assets</b></p> <p>The Board encouraged the IASB to resolve an inconsistency between IAS 27 and SIC-13 <i>Jointly Controlled Entities – Non-monetary Contributions by Venturers</i>: if a</p>	<p>Not raised explicitly in the ED.</p> <p>Paragraph BC21 noted that the SIC-13 consensus concerning contributions of non-monetary assets is consistent with requirements in the existing IAS 28 (para 22)</p>	<p>Paragraph B34: gains/losses on sales or contributions of assets to a <u>joint operation</u> are recognised only to the extent of the other parties’ interests.</p> <p>The revised IAS 28 now covers sales/contributions of assets to a <u>joint venture</u> with limited gain/loss</p>

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<p>subsidiary is contributed by a party to a joint arrangement, IAS 27 requires recognition of the full gain/loss due to the loss of control whereas SIC-13 gain/loss recognition is limited to the extent of the interests attributable to the other parties to the joint arrangement.</p>	<p>for transactions with associates.</p>	<p>recognition, under the equity method of accounting.  <u>Staff view</u> – issue remains, but it is an existing issue.                      Limited impact expected; the IASB intends to deal with the issue at some stage. Await that process.</p>
<p><b>Foreign currency translation</b>                      The Board noted diversity in application of IAS 21 <i>The Effects of Changes in Foreign Currency Exchange Rates</i> by parties that participate in a joint operation but do not share in joint control. The issue concerns whether their interest in the joint operation can be characterised as a ‘foreign operation’ (e.g. as a branch) for the purposes of foreign currency translation accounting.</p>	<p>This issue was not raised in the ED.</p>	<p>The issue has not been addressed in the new Standards, nor mentioned in Bases for Conclusions. Consequential amendments to IAS 21 do not address this matter.  <u>Staff view</u> – issue remains, but it is an existing issue. Could be addressed in the context of any revision of IAS 21, included in annual improvements, or referred to the IFRS Interpretations Committee.</p>