

Urgent Issues Group

Interpretation 113

July 2004

Jointly Controlled Entities – Non-Monetary Contributions by Venturers



Australian Government

**Australian Accounting
Standards Board**

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PREFACE

Reasons for Issuing UIG Interpretation 113

The Australian Accounting Standards Board (AASB) is implementing the Financial Reporting Council's policy of adopting the Standards of the International Accounting Standards Board (IASB) for application to reporting periods beginning on or after 1 January 2005. The AASB has decided it will continue to issue sector-neutral Standards, that is, Standards applicable to both for-profit and not-for-profit entities, including public sector entities. Except for Standards that are specific to the not-for-profit or public sectors or that are of a purely domestic nature, the AASB is using the IASB Standards as the "foundation" Standards to which it adds material detailing the scope and applicability of a Standard in the Australian environment. Additions are made, where necessary, to broaden the content to cover sectors not addressed by an IASB Standard and domestic, regulatory or other issues.

The same approach applies to UIG pronouncements. This Interpretation is part of the set of Australian equivalents to each International Accounting Standard (IAS), International Financial Reporting Standard (IFRS) and Interpretation of the IASB (collectively defined by the IASB as IFRSs). This set includes UIG Interpretations that correspond to the IASB Interpretations originated by the International Financial Reporting Interpretations Committee (IFRIC) or the former Standing Interpretations Committee (SIC).

Main Features of this Interpretation

This Interpretation is applicable to annual reporting periods beginning on or after 1 January 2005. To promote comparability among the financial reports of Australian entities, early adoption of this Interpretation is not permitted.

Application of this Interpretation will begin in the first annual reporting period beginning on or after 1 January 2005 in the context of adopting all Australian equivalents to IFRSs. The requirements of Accounting Standard AASB 1 *First-time Adoption of Australian Equivalents to International Financial Reporting Standards*, the Australian equivalent of IFRS 1 *First-time Adoption of International Financial Reporting Standards*, must be observed. AASB 1 requires prior period information, presented as comparative information, to be restated as if the requirements of this Interpretation had always applied. This differs from previous Australian requirements where changes in accounting policies did not require the restatement of the income statement and balance sheet of the preceding period.

This Interpretation addresses accounting for gains and losses made in respect of non-monetary contributions by a venturer to a jointly-controlled entity and

the presentation of any unrealised gains or losses in the consolidated financial statements of the venturer.

The Interpretation requires a venturer to recognise gains or losses on contributions of non-monetary assets to a jointly-controlled entity to the extent of the equity interests of the other venturers, except in certain circumstances when the entire gain or loss is regarded as unrealised. A venturer is required to recognise its share of previously unrealised gains or losses as the jointly-controlled entity consumes or sells the contributed assets and, if not recognised by then, when it disposes of its interest in the jointly-controlled entity.

Comparison with Superseded Requirements

Interpretation 113 supersedes Abstract 36 *Non-Monetary Contributions Establishing a Joint Venture Entity*. Although the requirements are substantially similar, there are some differences between the Interpretation and the Abstract. The principal difference is that whereas Abstract 36 did not include exceptions to the requirement for the proportionate recognition of gains or losses on contributions of non-monetary assets, this Interpretation includes three circumstances in which all of the gain or loss is regarded as unrealised. For example, Interpretation 113 may differ from Abstract 36 in respect of the treatment of contributions of non-monetary assets similar to those contributed by other venturers. Whereas Abstract 36 required such contributions to be measured at fair value and the recognition of the venturer's proportionate share of the gain or loss, Interpretation 113 prohibits the recognition of a gain or loss where the contribution of similar assets lacks commercial substance.

A further difference is that Abstract 36 required unrealised losses not to be eliminated to the extent that the transaction provided evidence of impairment. Interpretation 113 does not address this, because AASB 131 *Interests in Joint Ventures* requires the full amount of any loss to be recognised when the transaction provides evidence of impairment.

COMPARISON WITH INTERNATIONAL PRONOUNCEMENTS

UIG Interpretation 113 is equivalent to Standing Interpretations Committee Interpretation SIC-13 *Jointly-Controlled Entities – Non-Monetary Contributions by Venturers*, issued by the IASB. Paragraphs that have been added to this Interpretation (and do not appear in the text of the equivalent SIC Interpretation) are identified with the prefix “Aus”, followed by the number of the relevant SIC paragraph and decimal numbering.

Interpretation 113 is based on the equity method of accounting for interests in jointly-controlled entities in accordance with the requirements of AASB 131. Unlike IAS 31 *Interests in Joint Ventures*, AASB 131 does not permit use of the proportionate consolidation method of accounting for interests in jointly-controlled entities.

Interpretation 113 specifies when a venturer recognises unrealised profits or losses that have been eliminated under the equity method of accounting. This is not dealt with explicitly in SIC-13. However, IAS 31 deals with when a venturer recognises its share of profits or losses of a joint venture where the venturer sells assets to or purchases assets from the joint venture. The requirements are consistent.

Entities that comply with Interpretation 113 will simultaneously be in compliance with SIC-13.

International Public Sector Accounting Standards (IPSASs) are issued by the Public Sector Committee of the International Federation of Accountants. There is no IPSAS equivalent to Interpretation 113. However, IPSAS 8 *Financial Reporting of Interests in Joint Ventures* (May 2000) contains similar requirements to AASB 131 in respect of the recognition of gains and losses on contributions or sales to a joint venture by a venturer.

URGENT ISSUES GROUP

INTERPRETATION 113

JOINTLY CONTROLLED ENTITIES – NON-MONETARY CONTRIBUTIONS BY VENTURERS

ISSUE

1. Accounting Standard AASB 131 *Interests in Joint Ventures*, paragraph 48, refers to both contributions and sales between a venturer and a joint venture as follows: “When a venturer contributes or sells assets to a joint venture, recognition of any portion of a gain or loss from the transaction shall reflect the substance of the transaction.” In addition, AASB 131.24 says that “a jointly controlled entity is a joint venture that involves the establishment of a corporation, partnership or other entity in which each venturer has an interest.” There is no explicit guidance on the recognition of gains and losses resulting from contributions of non-monetary assets to jointly controlled entities (“JCEs”).
2. Contributions to a JCE are transfers of assets by venturers in exchange for an equity interest in the JCE. Such contributions may take various forms. Contributions may be made simultaneously by the venturers either upon establishing the JCE or subsequently. The consideration received by the venturer(s) in exchange for assets contributed to the JCE may also include cash or other consideration that does not depend on future cash flows of the JCE (“additional consideration”).
3. The issues are:
 - (a) when the appropriate portion of gains or losses resulting from a contribution of a non-monetary asset to a JCE in exchange for an equity interest in the JCE should be recognised by the venturer in the income statement;
 - (b) how additional consideration should be accounted for by the venturer; and
 - (c) how any unrealised gain or loss should be presented in the consolidated financial statements of the venturer.

4. This Interpretation deals with the venturer's accounting for non-monetary contributions to a JCE in exchange for an equity interest in the JCE that is accounted for using the equity method.

CONSENSUS

5. **In applying AASB 131.48 to non-monetary contributions to a JCE in exchange for an equity interest in the JCE, a venturer shall recognise in profit or loss for the period the portion of a gain or loss attributable to the equity interests of the other venturers except when:**
 - (a) **the significant risks and rewards of ownership of the contributed non-monetary asset(s) have not been transferred to the JCE;**
 - (b) **the gain or loss on the non-monetary contribution cannot be measured reliably; or**
 - (c) **the contribution transaction lacks commercial substance, as that term is described in AASB 116 *Property, Plant and Equipment*.**

If exception (a), (b) or (c) applies, the gain or loss is regarded as unrealised and therefore is not recognised in profit or loss unless paragraph 6 also applies.

6. **If, in addition to receiving an equity interest in the JCE, a venturer receives monetary or non-monetary assets, an appropriate portion of gain or loss on the transaction shall be recognised by the venturer in profit or loss.**
7. **Unrealised gains or losses on non-monetary assets contributed to JCEs shall be eliminated against the investment under the equity method. Such unrealised gains or losses shall not be presented as deferred gains or losses in the venturer's consolidated balance sheet.**

- Aus7.1 Where a venturer has recognised a gain or loss in profit or loss under paragraph 5 or 6, the amount of the unrealised gain or loss that has been eliminated shall be recognised by the venturer as it is realised by the JCE (as the contributed assets are consumed or sold) or, if not already realised by the JCE, when the venturer disposes of its investment in the JCE.**

Application

- Aus7.2** This Interpretation applies when AASB 131 applies.
- Aus7.3** This Interpretation applies to annual reporting periods beginning on or after 1 January 2005.
- Aus7.4** This Interpretation shall not be applied to annual reporting periods beginning before 1 January 2005.
- Aus7.5** The requirements specified in this Interpretation apply to the financial report where information resulting from their application is material in accordance with AASB 1031 *Materiality*.
- Aus7.6** When applicable, this Interpretation supersedes Abstract 36 *Non-Monetary Contributions Establishing a Joint Venture Entity*, as issued in December 2000.
- Aus7.7** Abstract 36 remains applicable until superseded by this Interpretation.

DISCUSSION

8. AASB 131.48 requires that, while the assets are retained in the joint venture, the venturer should recognise only that portion of the gain or loss which is attributable to the interests of the other venturers. Additional losses are recognised if required by AASB 131.48.
9. AASB 131.48 refers to the transfer of the “significant risks and rewards of ownership” as a condition for recognition of gains or losses resulting from transactions between venturers and joint ventures. AASB 118 *Revenue*, paragraphs 16(a) to (d), contain examples of situations where the risks and rewards of ownership are typically not transferred. This guidance also applies by analogy to the recognition of gains or losses resulting from contributions of non-monetary assets to JCEs. Since the venturer participates in joint control of the JCE, it retains some “continuing managerial involvement” in the asset transferred. However, this does not generally preclude the recognition of gains or losses since joint control does not constitute control to the degree usually associated with ownership (AASB 118.14(b)).
10. Paragraph 92 of the *Framework for the Preparation and Presentation of Financial Statements* states: “income is recognised in the income statement when an increase in future economic benefits related to an increase in an asset or a decrease of a liability has arisen that can be

measured reliably.” AASB 118.14(c) requires, among other conditions, that revenue from the sale of goods should be recognised when “the amount of revenue can be measured reliably”. The requirement for reliable measurement also applies to the recognition of gains or losses resulting from a contribution of non-monetary assets to a JCE.

11. AASB 118.12 explains that “when goods and services are exchanged or swapped for goods or services which are of similar nature and value, the exchange is not regarded as a transaction which generates revenue.”¹ The same rationale applies to a contribution of non-monetary assets since a contribution to a JCE is, in substance, an exchange of assets with the other venturers at the level of the JCE.
12. To the extent that the venturer also receives cash or non-monetary assets dissimilar to the assets contributed in addition to equity interests in the JCE, the realisation of which is not dependent on the future cash flows of the JCE, the earnings process is complete. Accordingly, the appropriate portion of the gain on the non-monetary contribution is recognised in profit or loss for the period.
13. It is not appropriate to present unrealised gains or losses on non-monetary assets contributed to JCEs as deferred items since such items do not meet the recognition criteria for assets or liabilities as defined in the *Framework* (paragraphs 53 to 64 and paragraphs 89 to 91).

Date of SIC’s Consensus: [Deleted by the UIG]

Effective Date of SIC-13: [Deleted by the UIG]

14. [Deleted by the UIG]

15. [Deleted by the UIG]

¹ AASB 116 requires an entity to measure an item of property, plant and equipment acquired in exchange for a non-monetary asset or assets, or a combination of monetary and non-monetary assets, at fair value unless the exchange transaction lacks commercial substance.

REFERENCES

Australia

The Urgent Issues Group discussed Issues Paper UIG/SIC 04/1 “Adoption of Various SIC Interpretations in Australia” in relation to this Interpretation at its meeting on 4 May 2004.

Accounting Standard AASB 116 *Property, Plant and Equipment*

Accounting Standard AASB 118 *Revenue*

Accounting Standard AASB 131 *Interests in Joint Ventures*

Framework for the Preparation and Presentation of Financial Statements

International Accounting Standards Board

International Accounting Standard IAS 31 *Interests in Joint Ventures*

Standing Interpretations Committee Interpretation SIC-13 *Jointly Controlled Entities – Non-Monetary Contributions by Venturers*

IFAC Public Sector Committee

International Public Sector Accounting Standard IPSAS 8 *Financial Reporting of Interests in Joint Ventures*