Accounting Standard

AASB 1016
August 1998

Accounting for Investments in Associates

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Australian Accounting Standards Board

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Defined words appear in *italics* the first time they appear in a section. The definitions are in Section 9. Standards are printed in **bold** type and commentary in light type.

MAIN FEATURES OF THE STANDARD

The Standard:

(a) defines associates and prescribes the circumstances in which investors must use the equity method of accounting for investments in associates

(b) prescribes rules for the implementation of the equity method of accounting under which:

  (i) the carrying amount of the investment is increased or decreased to recognise the investor's share of the post-acquisition profits or losses and other changes in net assets of the associate

  (ii) the investor's share of the post-acquisition profits or losses of the associate is included in the consolidated profit and loss statement of the investor

(c) prescribes disclosure requirements in respect of investments in associates, including those for which the equity method of accounting is not required.

ACCOUNTING STANDARD AASB 1016

The Australian Accounting Standards Board makes Accounting Standard 1016 "Accounting for Investments in Associates" under section 334 of the *Corporations Law 1998*

Dated 24 August 1998

K H Spencer
Director – AASB

ACCOUNTING STANDARD

AASB 1016 "ACCOUNTING FOR INVESTMENTS IN ASSOCIATES"

1 Application

1.1 Subject to paragraph 1.2, this Standard applies to each *entity* which is required to prepare financial reports in accordance with Part 2M.3 of the Corporations Law and which:

(a) is a *reporting entity*; or

(b) holds those financial reports out to be, or form part of, a *general purpose financial report.*

1.1.1 The standards specified in this Standard apply to the financial report where information resulting from their application is material. This requirement is set out in Accounting Standard AASB 1031 "Materiality", which provides guidance on the role of materiality in making judgements in the preparation and presentation of financial reports.

1.2 Except for the requirements of paragraph 6.1, this Standard does not apply where, in accordance with another Accounting Standard, investments are measured at *net market value* and changes in net market value are *recognised* as revenues or expenses in the profit and loss statement in the *financial year* in which the changes occur.

1.2.1 Paragraph 6.1 of this Standard requires certain disclosures to be made about all *associates* whether the *investor* applies the equity method or the net market value method of accounting for investments.

1.2.2 The other requirements of this Standard do not apply where the net market value method of accounting for investments is required by or adopted in accordance with another Accounting Standard. For example, Accounting Standard AASB 1023 "Financial Reporting of General Insurance Activities" requires the net market value method of accounting to be applied for investments that are integral to general insurance activities. Another example is Accounting Standard AASB 1030 "Application of Accounting Standards to Financial Year Accounts and Consolidated Accounts of Disclosing Entities other than Companies", which permits undertakings to which prescribed interests relate to apply the net market value method of accounting for financial assets.

2 Operative Date

2.1 This Standard applies to *financial years* beginning on or after 1 July 1998.

2.1.1 The recognition and measurement requirements of this Standard apply to half-year financial reports for half-years beginning on or after 1 July 1998.

2.2 This Standard may be applied to financial years beginning before 1 July 1998 where an election has been made in accordance with subsection 334(5) of the Corporations Law.

2.3 When operative, this Standard supersedes Accounting Standard AASB 1016 "Disclosure of Information about Investments in Associated Companies" as approved by notice published in *Commonwealth of Australia Gazette* No. S224 on 29 June 1989 and amended by Accounting Standard AASB 1025 "Application of the Reporting Entity Concept and Other Amendments".

2.3.1 Notice of this Standard was published in the *Commonwealth of Australia Gazette* on 25 August 1998.

3 Purpose of Standard

3.1 The purpose of this Standard is to:

(a) prescribe the circumstances in which *investors* must use the equity method of accounting ("equity method") for investments in *associates*

(b) prescribe how the equity method is to be applied

(c) require certain disclosures in respect of investments in associates.

3.1.1 In some cases, the relationship between an investor and its *investee* does not extend beyond an investor/investee relationship. However, in other cases, a special relationship between the investor and the investee exists which is characterised by the investor's control of, or *significant influence* over, an investee. This Standard deals with circumstances where an investor has significant influence over an investee. In these cases, the investee is known as an associate. Accounting Standard AASB 1024 "Consolidated Accounts" deals with accounting for controlled *entities* (*subsidiaries*).

3.1.2 Where the investor has significant influence over the investee, it has the *capacity* to affect substantially either, or both, the investee's financial and operating policies. Consequently, the investor should be able to achieve some protection from changes in the operating and financing policies of the investee which would adversely affect it, and also achieve broad consistency, in areas of mutual interest, in the implementation of policies. In these circumstances, the investor has a measure of responsibility for the associate's performance. Since the associate's performance and the economic resources underlying the investment may have a significant effect on the investor, information about them should be reported in the financial report of the investor.

3.1.3 Under the equity method, the investment is initially recorded at the *cost of acquisition* and adjusted thereafter for post-acquisition changes in the investor's share of the net assets of the investee. The profit and loss statement reflects the investor's share of the *profit or loss* of the investee.

3.1.4 Prescribing the use of the equity method for investments in associates and the disclosures specified in this Standard should result in *general purpose financial reports* that reflect the importance of investments in associates to the activities of the investor. This information should assist users of the reports to assess the investor's performance, financial position and financing and investing activities.

4 Accounting for Investments in Associates

4.1 An *investor* that is required to prepare a consolidated financial report must *recognise* an investment in an *associate* by applying the equity method in its consolidated financial report and by applying the cost method of accounting ("cost method") in its own financial report.

4.1.1 In this Standard, the equity method is viewed as a method of determining the *carrying amount* of an investment in an associate and the amount of revenue from the investment. The general features of, and requirements for, the application of the equity method are set out in Section 5 of this Standard.

4.1.2 The general features of the cost method are:

(a) an investment in the *equity* of another *entity* is initially recognised at its *cost of acquisition*

(b) revenue attributable to the investment is recognised only to the extent of dividends received or receivable out of post-acquisition profits of the *investee*

(c) dividends received or receivable from pre-acquisition profits are considered to be a recovery of part of the cost of the investment and are accounted for by reducing the carrying amount of the investment

(d) the carrying amount of the investment may be revalued in accordance with Accounting Standard AASB 1010 "Accounting for the Revaluation of Non-Current Assets".

4.2 An investor that is not required to prepare a consolidated financial report must recognise an investment in an associate by applying the equity method in its own financial report.

5 Application of the Equity Method

Initial Application

5.1 When an investment in an *associate* is acquired, the investment must be *recognised* at its *cost of acquisition*.

5.1.1 The *carrying amounts* of the identifiable assets and liabilities of the associate are examined as at the *acquisition date* and, where appropriate, notionally adjusted to *fair values* as at that date. Any difference between the cost of the investment in the associate and the *investor's* share of the net adjusted fair values is regarded as goodwill (or, as the case may be, discount on acquisition). Notional adjustments are made to the *profit or loss* of the associate in subsequent periods to reflect revisions in depreciation of depreciable assets and any amortisation of goodwill. This Standard does not require the goodwill (discount on acquisition) relating to the associate to be disclosed separately in the consolidated financial report.

5.2 When an *investee* becomes an associate subsequent to initial acquisition of an *ownership interest*:

(a) the carrying amount of the investment must be adjusted to that amount, determined in accordance with paragraph 5.3, which would have been the carrying amount had it been an investment in an associate since the acquisition date

(b) the share of profits or losses of the associate since the acquisition date must be recognised in the profit and loss statement

(c) the share of movements in reserves of the associate other than retained profits or accumulated losses, such as asset revaluation reserves, which has not been previously recognised by the investor, must be recognised as part of reserves.

5.2.1 The purchase of an additional ownership interest or the occurrence of other events or transactions may result in an investor obtaining *significant influence* over an investee.

5.2.2 Where an investor obtains an ownership interest in an associate in discrete steps, say in two tranches of 10 per cent and 15 per cent respectively, the carrying amount of the investment is determined by applying the equity method in respect of each separate tranche as at the acquisition date of each tranche. The amount of the adjustment to the carrying amount of the investment which is recognised in the profit and loss statement is determined by reference to the investor's share of profit or loss of the investee, determined in accordance with paragraph 5.3(a), arising subsequent to the acquisition date of each particular tranche. These adjustments are illustrated in the Appendix to this Standard.

Subsequent Application

5.3 In each *financial year* that the equity method is applied, the carrying amount of the investment in the associate:

(a) must be increased or decreased by the amount of the investor's share of the post-acquisition profit or loss of the associate in relation to the financial year after adjustments for:

(i) distributions to preference equityholders

(ii) revisions in depreciation of depreciable assets and amortisation of goodwill arising from notional adjustments made as at the date of acquisition (see paragraph 5.1.1)

(iii) dissimilar accounting policies, in accordance with paragraph 5.9

(iv) certain inter-entity transactions, in accordance with paragraphs 5.10 and 5.11

(b) must be decreased by the amount of dividends received or receivable from the associate

(c) must be increased or decreased by the amount of the investor's share of post-acquisition increments or decrements in the associate's total reserves in relation to the financial year, to the extent that the amounts of these movements have not been recognised previously in the profit and loss statement of the associate, or otherwise reflected in the carrying amount of the investment.

5.3.1 If an associate has outstanding cumulative preference shares, the investor computes its share of the profit or loss of the associate after adjusting for preference dividends, whether or not dividends have been declared.

5.3.2 Under the cost method, the investor recognises dividends received or receivable from an associate as revenue in its own financial report. Under the equity method, dividends received or receivable from the associate must be deducted from the carrying amount of the investment so that recognition of this portion of the share of profits of the associate is not duplicated. A corresponding adjustment must be made so that the amount of revenue is not overstated.

5.3.3 Where the associate revalues all or some of its assets after the investor has acquired its ownership interest and that revaluation records asset values already reflected in the investor's cost of acquisition and thus the carrying amount of the investment, the carrying amount is not adjusted to reflect the movement in the asset revaluation reserve.

5.4 In each financial year that the equity method is applied:

(a) the amount of the investor's share of the post-acquisition profit or loss of the associate in relation to the financial year, determined in accordance with paragraph 5.3(a), must be recognised in the profit and loss statement

(b) the amount of the investor's share of the post-acquisition increments and decrements in the associate's reserves in relation to the financial year, determined in accordance with paragraph 5.3(c), must be recognised in the investor's reserves.

5.5 The investor's share of the net assets, the profit or loss and the reserves of an associate must be determined in accordance with the investor's ownership interest in the associate.

5.6 If the associate is a *parent entity*, the investor's share of the net assets, the profit or loss and the reserves of that associate must be based on the net assets, the profit or loss and the reserves of the *economic entity* attributable to members of the parent entity reflected in the associate's consolidated financial report.

Financial Reports of the Associate

5.7 In accounting for an associate, the investor must ensure that the most recent financial information available to the equityholders of the associate is used.

5.7.1 There may be constraints on the information which an investor may provide about an associate. For example, where an associate is a company, financial information may be limited to that provided in the most recent published financial report of the company. This information is readily available to all shareholders of the associate.

5.8 Where a difference exists between the *reporting date* of the associate and that of the investor, and it is not possible to bring the reporting dates into line, the difference must be consistent from financial year to financial year.

5.8.1 Where the financial report of the associate is prepared at a date earlier than that of the investor, it may be necessary to include additional information in the consolidated financial report by way of note. This note would disclose significant events or transactions which have occurred since the date of the associate's previous financial report where these events or transactions could materially affect the performance or financial position of the associate for the subsequent financial year.

Dissimilar Accounting Policies

5.9 Where the accounting policies adopted by an associate are dissimilar and are not required to be adopted by another Accounting Standard, and this dissimilarity would materially affect the amounts determined as the investor's share of the net assets, the profit or loss and the reserves of the associate, adjustments must be made, where possible, to achieve consistency with the accounting policies of the investor.

Inter-Entity Transactions

5.10 Adjustments must be made, where possible, to eliminate unrealised profits and unrealised losses on transactions between the associate and:

(a) the investor and its controlled *entities* (the economic entity);

(b) another associate of the investor.

5.11 Where a transaction is between an entity within the economic entity and an associate, the amount of the unrealised profits or unrealised losses eliminated must be determined in accordance with the investor's ownership interest in the associate. Where a transaction is between associates of the investor, the amount of the unrealised profits or unrealised losses eliminated must be determined in accordance with the product of the investor's ownership interest in each of the associates.

5.11.1 Where, for example, an associate in which a 25% ownership interest is held transacts with an associate in which a 40% ownership interest is held, 10% (0.25 x 0.4) of the unrealised profit or unrealised loss is eliminated.

Discontinuation of the Equity Method

5.12 The equity method must not be applied when an investee ceases to qualify as an associate because the investor's influence over the investee has been reduced. Thereafter, where the investment is retained, it must be accounted for in accordance with the cost method. In these circumstances, the carrying amount of the investment determined by the equity method remains the carrying amount of the investment, and thereafter dividends from the investee must be recognised as revenue to the extent that they are not already reflected in the carrying amount of the investment.

5.12.1 The investee ceases to qualify as an associate when the investor no longer has significant influence. This may occur for a number of reasons, including the sale of part of the investment and changes in the ownership structure of the investee. In the event that the investor acquires control of the investee, the requirements of Accounting Standard AASB 1024 "Consolidated Accounts" apply.

5.13 The amount of an investor's share of the losses and reserve decrements of an associate must be recognised in their entirety. However, where the investor's share of losses and reserve decrements reduces the carrying amount of the investment below zero, application of the equity method must be discontinued and the investment recorded at zero.

5.14 When an investor resumes application of the equity method after having discontinued its use, the investor must not recognise its share of the profits and reserve increments of the associate until such share offsets its share of losses and reserve decrements not recognised during the financial years in which the equity method was not applied.

Carrying Amount of the Investment

5.15 The carrying amount of an investment in an associate must not exceed its *recoverable amount.* Where the recoverable amount of an investment has declined below its carrying amount, the carrying amount must be written down to that recoverable amount. The amount of the reduction must be recognised in the profit and loss statement in the financial year in which the reduction occurs.

5.15.1 Where equity instruments are traded in an active and liquid market, the quoted market price is normally regarded as a reliable indicator of the recoverable amount. Where there is infrequent activity in a market, or the market is not well established, or small volumes are traded relative to the size of the investor's holding in the investee, quoted market prices may not be a reliable indicator of the recoverable amount of the investment in the associate. In these circumstances, as well as when a quoted market price is not available, estimation techniques, which include discounted cash flow techniques, may need to be used to estimate the recoverable amount. In applying discounted cash flow techniques a current market-determined risk-adjusted discount rate which reflects such factors as the expected rate of return prevailing in the market for an investment having a similar exposure to business, credit and market risk should be used.

5.16 Where an investment in an associate has been written down to recoverable amount as at a previous reporting date in accordance with paragraph 5.15, the write-down must be reversed to the extent that the recoverable amount as at the current reporting date exceeds the written-down carrying amount. The amount of the reversal must be recognised in the profit and loss statement in the financial year in which the reversal occurs.

5.17 Where the equity method is applied, the maximum amount at which an investment in an associate can be recognised in the consolidated financial report is the carrying amount determined by applying the equity method.

5.17.1 The application of the equity method precludes the recognition of increases in the carrying amount of the investment through revaluations made in accordance with Accounting Standard AASB 1010 "Accounting for the Revaluation of Non-Current Assets".

Reciprocal Equity Holdings Between Investor and Associate

5.18 Where an associate holds *equity* in the investor, the carrying amount of the investment in the associate must be reduced by an amount representing the investor's indirect holding in its own equity because of the cross-holding. An equivalent adjustment must be made to the equity of the investor.

5.19 Where an associate holds equity in the investor and uses the cost method to account for its investment, the amount of the investor's share of the associate's profit or loss must be determined after eliminating from the associate's profit or loss dividends received or receivable by the associate from the investor included therein.

5.20 Where an associate holds equity in the investor and uses the equity method to account for its investment, the amount of the investor's share of the associate's profit or loss must be determined after eliminating the effect of the associate having applied the equity method to determine the carrying amount of its investment in the investor.

5.20.1 The purpose of the adjustments in paragraphs 5.19 and 5.20 is to eliminate, from the investor's share of the profit or loss of an associate, the investor's proportionate share of that part of its own profit or loss which has been included in the associate's profit or loss.

Changes in Investor's Ownership Interest

5.21 The carrying amount of an investment in an associate must be adjusted where the investor's ownership interest in the associate is reduced by sale of part of that interest, or in consequence of a post-acquisition change in the equity of the associate.

5.22 Where the transactions or events referred to in paragraph 5.21 result in a change in the share of retained profits or accumulated losses of an associate, the carrying amount of the investment must be adjusted and the amount of the change must be recognised in the profit and loss statement.

5.23 Where the transactions or events referred to in paragraph 5.21 result in a change in the share of reserves other than retained profits or accumulated losses of an associate, the amount of the

change must be recognised as part of reserves and must not be recognised in the profit and loss statement.

5.24 A change in ownership interest resulting from further acquisition of equity in an associate must be recognised at the cost of the acquisition to the investor in accordance with paragraph 5.1.

6 Disclosures

6.1 The following information must be disclosed:

(a) in respect of each *associate*:

(i) its name and principal activities

(ii) the *investor's ownership interest* as at the associate's *reporting date* and, if different, at the investor's reporting date

(iii) the proportion of *voting power* held in the associate where different from the proportion of ownership interest held

(iv) the *carrying amount* of the investment

(v) its reporting date, if different from that of the investor

(b) the amount of the investor's share of associates':

(i) contingent liabilities

(ii) capital commitments contracted for

(iii) other expenditure commitments contracted for, other than for the supply of inventories

(c) the amount of the investor's contingent liabilities that arise because the investor is severally liable for all the liabilities of an associate

(d) where an associate holds *equity* in the investor, the percentage of equity held by the associate

(e) where investments in associates, either individually or in aggregate, are material to an evaluation of the operating performance and financial position of the investor, a summarised presentation of the *recognised* amounts of assets, liabilities and *profit or loss* of associates, either individually or in aggregate, as appropriate.

6.2 Where the equity method is applied to investments in associates, the following information must be disclosed:

(a) the amount of the investor's share of associates':

(i) operating profits or losses before income tax

(ii) income tax expense attributable to operating profits or losses

(iii) extraordinary items (net of income tax)

(b) the amounts of retained profits or accumulated losses as at the beginning and end of the *financial year* which are attributable to associates

(c) the amounts of other reserves as at the beginning and end of the financial year which are attributable to associates

(d) a schedule setting out the movements in the carrying amount of investments in associates, separately identifying the carrying amount as at the beginning and end of the financial year, and the amounts of new investments, disposals, share of profit or loss, dividends and other movements

(e) the financial effects of events or transactions which have occurred after the reporting date of an associate and which could materially affect the financial position or operating performance of that associate for the next financial year

(f) where adjustments to eliminate the effect of dissimilar accounting policies cannot be made, the nature of the dissimilarities.

7 Comparative Information

7.1 Information for the preceding corresponding *financial year* which corresponds to the disclosures specified for the current financial year in this Standard must be disclosed, except where, in respect of the financial year to which this Standard is first applied, the superseded Standard did not require corresponding information.

7.1.1 Disclosure of comparative information for the financial year to which this Standard is first applied is encouraged where the superseded Standard did not require corresponding information.

8 Transitional Provisions

8.1 The accounting policies required by this Standard must be applied as at the beginning of the *financial year* to which this Standard is first applied. The *carrying amount* of investments in *associates* must be adjusted, as at the beginning of the financial year to which this Standard is first applied, to that amount which would have been the carrying amount had the requirements of this Standard been applicable from the *acquisition date* of the investment in the associate. The amount of this adjustment which relates to:

(a) the accumulated share of profits or losses of associates since the acquisition date must be adjusted against retained profits or accumulated losses

(b) increments and decrements in reserves of associates, other than retained profits or accumulated losses, must be adjusted against the reserves of the investor.

8.2 Where an investment in an associate is *recognised* at a revalued amount, the asset revaluation reserve and the carrying amount of the investment must be adjusted to remove the effects of the revaluation prior to implementing the requirements of paragraph 8.1.

8.2.1 The purpose of these adjustments is to ensure that amounts attributable to the investor's share of the post-acquisition profits or losses recognised by the associate are included in retained profits or accumulated losses of the investor and not included in other reserves. Adjustments to achieve this outcome are necessary irrespective of the method of accounting previously applied in respect of the investment in an associate.

8.3 **Where an investment in an associate is recognised at a revalued amount and the asset revaluation reserve attributable to the investment has been used, the amount of the adjustment must be made against retained profits or accumulated losses as at the beginning of the financial year to which this Standard is first applied.**

8.4 **Where the retrospective application of the requirements of this Standard is not practicable, the amounts attributed to the carrying amount of investments in associates shall be deemed to have been determined in accordance with this Standard.**

9 Definitions

9.1 In this Standard:

acquisition date **means the date on which an** ***investor*** **acquires an** ***ownership interest*** **in the** ***equity*** **of an** ***investee*** **(The terms pre-acquisition and post-acquisition must be read as deriving from this definition.)**

associate **means an investee, not being:**

(a) a ***subsidiary*** **of the investor; or**

(b) a partnership of the investor; or

(c) an investment acquired and held exclusively with a view to its disposal in the near future (see paragraphs 9.1.1 and 9.1.2)

over which the investor has ***significant influence***

borrowing corporation **is defined in the Corporations Law**

capacity **means ability or power, whether direct or indirect, and includes ability or power that is presently exercisable as a result of, by means of, in breach of, or by revocation of, any of or any combination of the following:**

(a) trusts

(b) relevant agreements

(c) practices,

whether or not enforceable

***carrying amount* means, in relation to an asset, the amount at which the asset is *recognised* in the balance sheet as at the *reporting date* net of any provisions for depreciation, amortisation or diminution in value**

***company* is defined in the Corporations Law**

***cost of acquisition* means purchase consideration plus any costs incidental to the acquisition**

***economic entity* means a group of *entities* comprising the *parent entity* and each of its subsidiaries**

***entity* means any legal, administrative, or fiduciary arrangement, organisational structure or other party (including a person) having the *capacity* to deploy scarce resources in order to achieve objectives**

***equity* means the residual interest in the assets of the entity after deduction of its liabilities**

***fair value* means the amount for which an asset could be exchanged between knowledgeable, willing parties in an arm's-length transaction**

***financial year* is defined in the Corporations Law**

***general purpose financial report* means a financial report intended to meet the information needs common to users who are unable to command the preparation of reports tailored so as to satisfy, specifically, all of their information needs**

***holding company* is defined in the Corporations Law**

***investee* means an entity in which an investor has an ownership interest**

investor **means an entity that has an ownership interest in the equity of another entity**

listed corporation **is defined in the Corporations Law**

net market value **means, in relation to an asset, the amount which could be expected to be received from the disposal of the asset in an orderly market after deducting costs expected to be incurred in realising the proceeds of such a disposal**

ownership interest **means the percentage of equity interest held in an** ***associate*** **by an investor, whether such interests are held directly or indirectly through subsidiaries or associates, or through their respective nominees. The percentage of equity interest excludes interests which carry no right to participate beyond a specified amount in the distribution of the entity's profits or in the ultimate distribution of its assets**

parent entity **means an entity which controls another entity**

profit or loss **means, in relation to:**

(a) **an entity - the operating profit or loss and extraordinary items of the entity after applicable income tax expense**

(b) **an economic entity - the operating profit or loss and extraordinary items attributable to members of the parent entity of the economic entity after applicable income tax expense**

recognised **means reported on, or incorporated in amounts reported on, the face of the profit and loss statement or balance sheet (whether or not further disclosure of the item is made in notes)**

recoverable amount **means, in relation to an asset, the net amount that is expected to be recovered through the cash inflows and outflows arising from its continued use and subsequent disposal**

reporting date **means the end of the** ***financial year*** **to which the financial report relates**

***reporting entity* means an entity (including an *economic entity*) in respect of which it is reasonable to expect the existence of users dependent on *general purpose financial reports* for information which will be useful to them for making and evaluating decisions about the allocation of scarce resources, and includes but is not limited to the following:**

(a) a *listed corporation*

(b) a *borrowing corporation*

(c) a *company* which is not a subsidiary of a *holding company* incorporated in Australia and which is a subsidiary of a foreign company where that foreign company has its securities listed for quotation on a *stock market* or those securities are traded on a stock market

***significant influence* means the capacity of an entity to affect substantially (but not control) either, or both, of the financial and operating policies of another entity (see paragraphs 9.1.3 to 9.1.8)**

***stock market* is defined in the Corporations Law**

***subsidiary* means an entity which is controlled by a parent entity**

***voting power* means the voting rights attaching to equity interests of an associate but excludes voting rights which apply only in special or contingent circumstances.**

Associate

9.1.1 As defined in this Standard, the term associate includes joint ventures, other than partnerships, which involve the establishment of an entity, that is, a joint venture entity in which the investor has an ownership interest. Joint ventures which are not established as entities separate from the venturers do not qualify as associates. Accordingly, unincorporated joint ventures which involve the shared use of assets and other resources of the venturer are not associates. The method of accounting for participation in these joint ventures is set out in Accounting Standard AASB 1006 "Accounting for Interests in Joint Ventures".

9.1.2 An investment which has been acquired and continues to be held exclusively with a view to disposal in the near future is not an associate under this Standard. Such an investment is held exclusively for sale if a purchaser has been identified, or is being actively sought, and disposal is reasonably expected to occur within one year of its *acquisition date.*

Significant Influence

9.1.3 Whether an investor has significant influence over an investee will need to be decided in the light of the prevailing circumstances. The existence of significant influence depends upon substance and not merely form.

9.1.4 Significant influence will normally stem from the investor's *voting power* in the investee which is linked to the investor's ownership interest. In some cases this will be conclusive, while in other cases this will need to be supported by satisfying other conditions. In deciding whether the investor's voting power gives rise to significant influence over the investee, it may be necessary to consider the distribution of the balance of the voting power. For example, in the case of a company, whether the balance of the voting power is held in a few large equityholdings or distributed over a large number of small equityholdings needs to be considered in determining the capacity of the investor to exercise significant influence.

9.1.5 Where an investor holds 20 per cent or more of the voting power in an investee, this could lead to a presumption that the investor has significant influence over the investee in the absence of evidence to the contrary. However, this percentage is not an absolute cut-off point. In certain cases, an investee will qualify as an associate, notwithstanding that the investor's voting power in the investee is less than or has fallen below 20 per cent. The converse also applies.

9.1.6 Some of the factors which, singly or in combination, may indicate the existence of significant influence are:

(a) the investor's voting power in the investee

(b) representation on the investee's board of directors or equivalent governing body

(c) dependence on technical information

(d) economic dependency, including material transactions between investor and investee

(e) interchange of managerial personnel

(f) participation in decisions on the distribution or retention of the investee's profits

(g) participation, in other ways, in policy-making decisions of the investee.

9.1.7 It is unlikely that significant influence would exist or would continue to exist where an investee operates under severe long-term restrictions which impair significantly its ability to make distributions to the investor, for example, restrictions on the repatriation of dividends.

9.1.8 The investor's voting power in an associate needs to be distinguished from the investor's ownership interest in the equity of that associate. Voting power is important in determining whether significant influence exists. The investor's ownership interest in the equity of the associate is relevant when measuring the *carrying amount* of the investment based on the investor's share of the associate's *profit or loss* and net assets.

CONFORMITY WITH INTERNATIONAL AND NEW ZEALAND ACCOUNTING STANDARDS

Conformity with International Accounting Standards

As at the date of issue of this Standard, compliance with this Standard will ensure conformity with International Accounting Standard IAS 28 "Accounting for Investments in Associates", with the following exceptions:

(a) IAS 28 requires the equity method to be applied in the investor's own financial report where the equity method is applied in the consolidated financial report. This Standard requires the cost method to be applied in the investor's own financial report except where consolidated financial report is not required to be prepared. Consolidated financial report prepared in accordance with this Standard will, except as noted in (b) below, comply with the requirements of IAS 28.

(b) IAS 28 requires the carrying amount of an investment to be written down to its recoverable amount which is determined as the higher of its value in use and net selling value. This Standard requires that the carrying amount of the investment must not exceed its recoverable amount but does not specify how the recoverable amount is to be determined. The Australian Accounting Standards Board and the Public Sector Accounting Standards Board of the Australian Accounting Research Foundation have a current project on impairment of assets. This difference will be addressed in the context of that project.

Conformity with New Zealand Accounting Standards

As at the date of issue of this Standard, compliance with this Standard will ensure conformity with Statement of Standard Accounting Practice SSAP-8 "Accounting for Business Combinations", to the extent that it addresses accounting for associates, with the following exceptions:

(a) SSAP-8 precludes the equity method from being applied in the investor's own financial report. This Standard requires the equity method of accounting to be applied in the investor's own financial report when a consolidated financial report is not required to be prepared. In this latter circumstance, SSAP-8 requires the investor to adapt its own financial report to incorporate the information required or to present an additional profit and loss statement and balance sheet incorporating this information.

(b) SSAP-8 requires that where an investor has less than a 20 per cent interest in an investee, the associate must concur in writing that the investor is in a position to exert significant influence, before the equity method may be applied by the investor. This Standard does not contain a similar requirement.

(c) SSAP-8 requires goodwill to be separately recognised and reported in a consolidated financial report. This Standard requires goodwill to be identified and notional adjustments to be made for the amortisation of goodwill to determine the profit or loss recognised by the investor under the equity method.

(d) SSAP-8 requires an investment in an associate to be written down to fair value if its fair value is less than the carrying amount for other than a temporary period. This Standard provides that the carrying amount of an investment in an associate should not exceed its recoverable amount.

APPENDIX

INVESTEE BECOMING AN ASSOCIATE SUBSEQUENT TO INITIAL ACQUISITION

This Appendix forms part of the commentary and is provided for illustrative purposes only. The example in this Appendix illustrates the accounting treatment outlined in paragraph 5.2.2 of this Standard concerning an investee becoming an associate subsequent to the initial acquisition of an ownership interest by the investor.

Example: An investor acquired a ten per cent interest in an investee on 1 January 19X1 for $76,000. As at this date the fair value of the net assets of the investee were $700,000 and comprised paid-up capital $500,000, asset revaluation reserve of $100,000 and retained profits of $100,000. A further fifteen per cent interest was acquired on 31 December 19X3 for $168,000. Significant influence is achieved on 31 December 19X3. At this date the fair value of the net assets of the investee were $920,000 and comprised paid-up capital $500,000, asset revaluation reserve $200,000 and retained profits $220,000. The investor had applied the cost method to account for its investment made on 1 January 19X1.

The investee, which had revalued its non-current assets as at 31 December 19X2, reported profits of $80,000, $60,000, and $100,000 in the years ended December 19X1, 19X2 and 19X3 respectively. Dividends from post-acquisition profits received by the investor were $4,000 in each year.

The amount of the adjustment made at 31 December 19X3 would be determined as follows:

(a) Acquisition of 10% interest: 1 January 19X1

Consideration paid	$76,000
Share of net assets acquired	70,000
Goodwill	$ 6,000

The investor's accounting policy is to amortise goodwill over three years.

(b) Acquisition of 15% interest: 31 December 19X3

Consideration paid	$168,000
Share of net assets acquired	138,000
Goodwill	$ 30,000

At 31 December 19X3 the carrying amount of the investment in the books of the investor would be $244,000 ($76,000 + $168,000) under the cost method. For the consolidated financial report, or the investor's own financial report if it is not a parent, the carrying amount would be adjusted as follows:

	Debit	Credit
	$	$
Investment	16,000	
Profit and Loss		6,000
Asset Revaluation Reserve		10,000

The change in the carrying amount of the investment arises from:

(i)	restating recognised revenues as an adjustment to investments in associates	
	Dividends received or receivable	$(12,000)
(ii)	recognition of the share of profits post-acquisition of tranche 1, now to be equity accounted	
	$240,000 x 10%	24,000
	Less: adjustments to reflect amortisation of goodwill since acquisition	
	$2,000 per year for 3 years	(6,000)
	Net adjustment to the profit and loss	$6,000
(iii)	recognition of the share of the movement in asset revaluation reserve occurring post-acquisition of tranche 1 and now to be equity accounted	
	$100,000 x 10%	10,000
	Total increase in the equity-accounted carrying amount of the investment	$16,000

DEVELOPMENT OF THE STANDARD

This section does not form part of the Standard. It is a summary of the development of the Standard and the Australian Accounting Standards Board's consideration of the key issues dealt with in the Standard.

1. In May 1997 the Board issued, but did not formally make, Proposed Revised Accounting Standard AASB 1016 "Accounting for Investments in Associates" because the legal impediment to equity accounting had not been removed. On 5 June 1997 the Australian Securities Commission issued a Class Order and Exemption under which reporting entities were relieved from applying Accounting Standard AASB 1016 "Disclosure of Information about Investments in Associated Companies" if they complied with all of the requirements in the Proposed Revised Accounting Standard. The legal impediment to equity accounting was removed by the *Company Law Review Act 1998* which came into effect on 1 July 1998.

2. The issue of the Standard follows consideration of the responses received on Exposure Draft ED 71 "Accounting for Investments in Associates by the Equity Method" which was prepared by the Australian Accounting Standards Board and by the Public Sector Accounting Standards Board of the Australian Accounting Research Foundation and released in December 1995.

3. The intention of ED 71 was to revise Accounting Standard AASB 1016 "Disclosure of Information about Investments in Associated Companies" to require investments in associates to be recognised in the financial report at amounts determined in accordance with the equity method. The superseded Standard AASB 1016 required disclosure of information determined in accordance with the equity method by way of note.

Noteworthy Differences from ED 71

4. ED 71 proposed a broad definition of "associates" and that the equity method be applied in respect of all associates. The Standard clarifies that the equity method is not required to be applied where, in accordance with another Accounting Standard, or as permitted by another Accounting Standard, the net market value method of accounting is used to account for an investment in an associate. In addition, the definition of an associate was amended to exclude:

   (a) an investment acquired and held exclusively with a view to disposal in the near future

(b) partnerships.

International Accounting Standard IAS 31 "Financial Reporting of Interests in Joint Ventures", which deals with accounting for joint venture entities, contains a benchmark treatment and an allowed alternative treatment. The benchmark treatment requires the proportionate consolidation method to be applied in accounting for interests in joint venture entities. The allowed alternative treatment permits the use of the equity method of accounting for interests in joint venture entities. This Standard requires the equity method of accounting to be applied where a joint venture entity is an associate of the investor.

This Standard does not prevent the equity method of accounting from being applied in accounting for interests in partnerships in the investor's own financial report.

5. ED 71 did not specify how to account for the adjustment arising when an investee becomes an associate subsequent to the initial acquisition of an ownership interest by the investor. Respondents sought clarification of the treatment of the adjustment. The Board considered requiring that the adjustment be:

(a) made to retained profits as at the beginning of the financial year; or

(b) recognised in the profit and loss account in the financial year in which the investee became an associate.

Accounting Standard AASB 1018 "Profit and Loss Accounts" precludes making an adjustment to retained profits as at the beginning of the financial year in these circumstances. As a result, the Standard requires that the adjustment relating to the accumulated share of post-acquisition profits or losses be recognised in the consolidated profit and loss statement.

6. ED 71 proposed that the carrying amount of an investment in an associate should not exceed its net market value. However, the Board concurred with the views of most respondents that the reference point for assessing the carrying amount of an equity-accounted investment should be consistent with that used for assessing other non-current assets. Accordingly, the Standard specifies that the carrying amount should not exceed the recoverable amount of the investment. The Standard also clarifies that where the equity method is applied the investment cannot be revalued upwards in accordance with Accounting Standard AASB 1010 "Accounting for the Revaluation of Non-Current Assets".

7. Some respondents commented that the transitional provisions in ED 71 did not deal specifically with circumstances where the carrying amount of an investment in an associate had previously been determined at a revalued amount and sought clarification of the accounting adjustments required on adopting the equity method. In response to these comments, the Standard now requires that the amount of the investment in an associate included in the consolidated financial report of the investor be adjusted to the amounts which would have been the carrying amount of the investment in the associate had the requirements of the Standard been applicable from the date of the investment in the associate. The effects of previous revaluations of the investment in the associate are required to be reversed prior to implementing the equity method. Where the asset revaluation reserve has been used, for example for making an issue of bonus shares, the transitional adjustment should be made against retained profits or accumulated losses.

Principal Features of ED 71 Retained in the Standard

8. The Standard retains the basic structure and content of the proposals in ED 71 relating to the recognition and measurement of investments in associates and the matters required to be disclosed.

9. Some respondents to ED 71 expressed the view that the equity method is a consolidation technique for reporting information about an investor, its subsidiaries and its associates as an economic entity. Those respondents to ED 71 noted that their view is consistent with the rationale underlying some overseas pronouncements that deal with the equity method. While this view is inconsistent with the concept of an economic entity as applied in Australia and the application of the criterion of control for determining the entities which should be consolidated as part of a reporting entity, as set out in Statement of Accounting Concepts SAC 1 "Definition of the Reporting Entity", the Board concurred with the views of respondents that implementation of the equity method is necessary to enable Australian reporting entities to report in a manner consistent with foreign national and international requirements and practice.

10. The treatment of reciprocal equityholdings between the investor and the associate on the carrying amount of the investment and the aggregate equity of the investor was implicit in ED 71. This Standard clarifies that the effect of the investor's indirect ownership in itself is to be eliminated.