

Joint Arrangements

Ind AS 111

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- ▶ Joint arrangements
- ▶ Classification of a joint arrangement
- ▶ Accounting treatment
- ▶ Continuous assessment
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- ▶ Disclosure
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- ▶ Difference between Ind AS111 and AS 27

Objectives and Scope

Objectives and Scope

Objective

The objective of this Ind AS is to establish principles for financial reporting by entities that have an interest in arrangements that are controlled jointly (i.e. joint arrangements).

Scope

This Ind AS shall be applied by all entities that are a party to a joint arrangement.

Joint arrangements

Joint arrangements

Definition

A joint arrangement is an arrangement over which two or more parties have joint control

- ▶ A joint arrangement is either a joint operation or a joint venture and has the following characteristics:
 - ▶ The parties are bound by a contractual arrangement
 - ▶ That contractual arrangement gives two or more of those parties joint control of the arrangement
- ▶ Contractual arrangement defines the terms
 - ▶ Often, but not always, in writing
 - ▶ Documented discussions
 - ▶ Law or articles of association

Joint arrangements

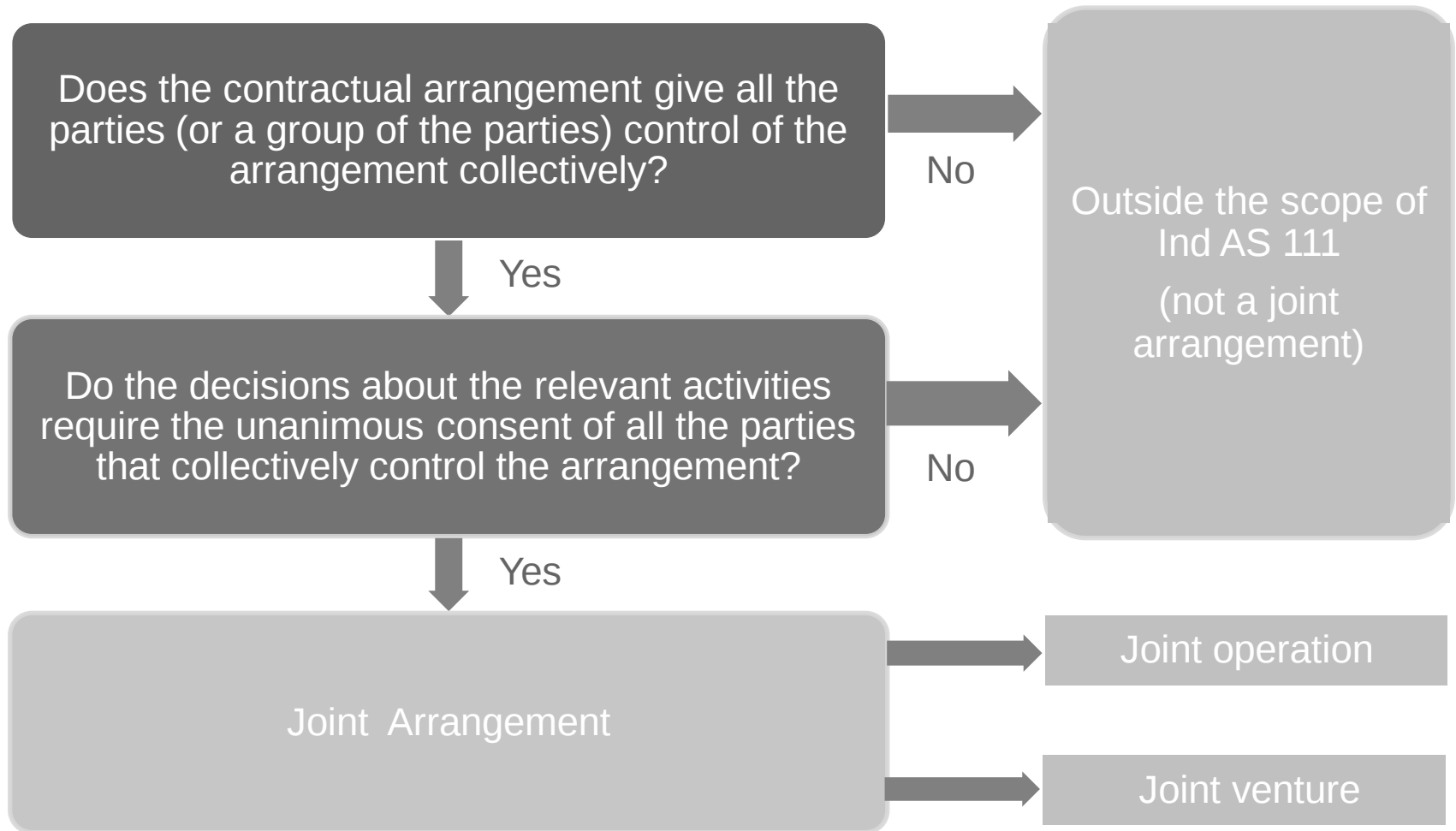
Joint control

Joint control is the contractually agreed sharing of *control* of an arrangement , which exists only when the decisions about the *relevant activities* require the *unanimous consent* of the parties sharing control

- ▶ Control (as defined by Ind AS 110): the investor is exposed, or has rights, to variable returns from its involvement with the investee and has the ability to affect those returns through its power over the investee
- ▶ Relevant activities: the activities of the arrangement that significantly affect the investee's returns
- ▶ Unanimous consent: no single party controls the arrangement and two or more parties must agree to share control

Joint arrangements

Joint control



Joint arrangements

Joint control - Examples

	Example 1	Example 2	Example 3
Requirement	75% vote to direct relevant activities	75% vote to direct relevant activities	Majority vote to direct relevant activities
Party A	50%	50%	35%
Party B	30%	25%	35%
Party C	20%	25%	Widely dispersed
Conclusion			

Joint arrangements

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Joint arrangements

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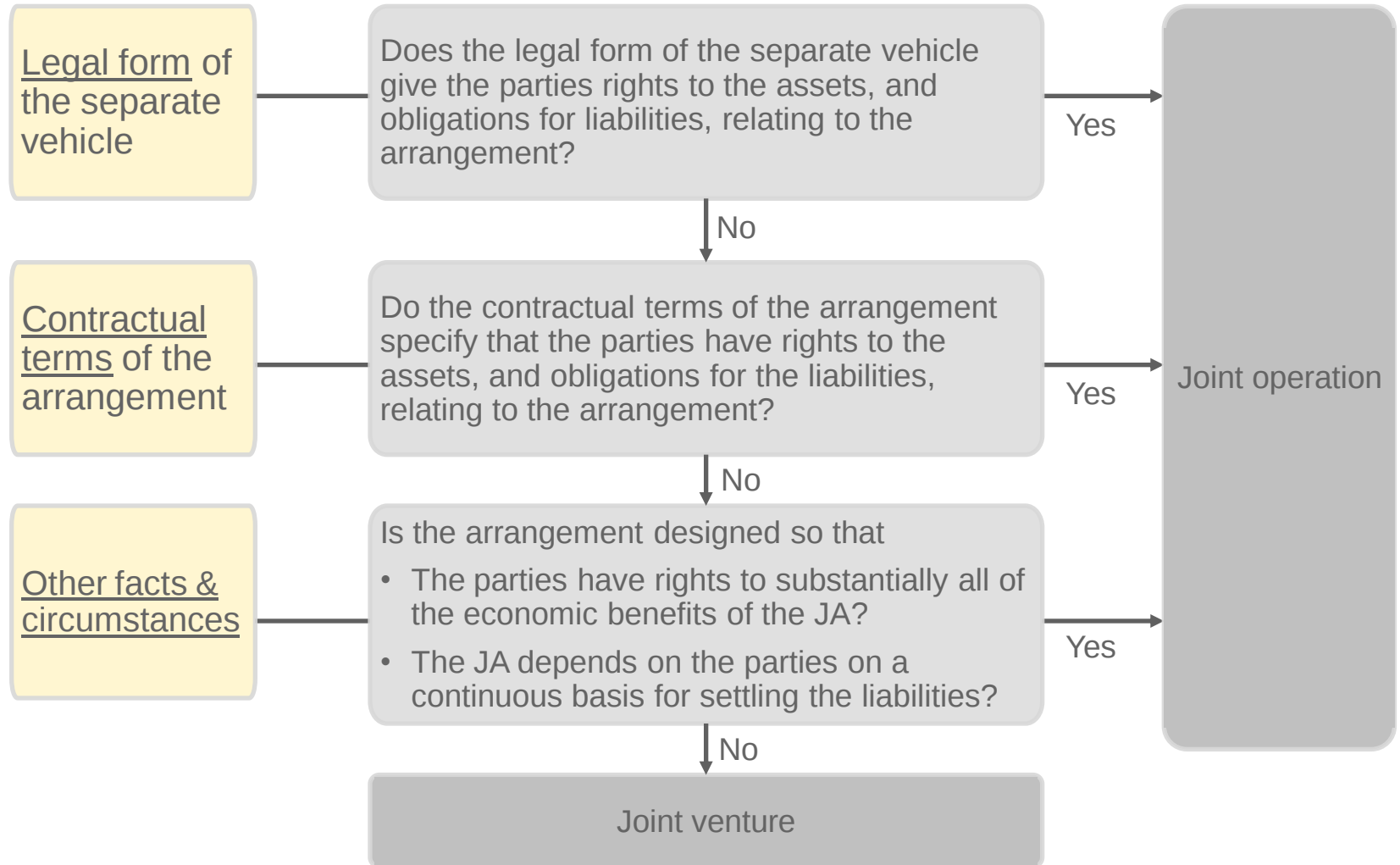
Joint arrangements

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Classification of a joint arrangement

Classification of a joint arrangement



Classification of a joint arrangement

Legal form

- ▶ Legal form is no longer the sole factor, but is still very important in classifying a joint arrangement

Joint Operations	Joint Ventures
Without a separate vehicle, the joint arrangement is a joint operation	To be a joint venture, there must be a separate vehicle
Parties have rights to the assets and obligations for the liabilities of the arrangement	Parties have rights to the net assets of the arrangement
The legal form of the separate vehicle does <u>not</u> confer separation between the parties and the separate vehicle (e.g., general partnership)	The legal form of the separate vehicle causes it to be considered in its own right (e.g., corporation)

- ▶ Separate vehicle: A separately identifiable financial structure, including separate legal entities or entities recognised by statute, regardless of whether those entities have a legal personality

Classification of a joint arrangement

Legal form - Example

▶ Fact pattern:

- ▶ A and B jointly establish a new corporation (C) in which each party has a 50% ownership interest
- ▶ Incorporation enables the separation of C from A and B
- ▶ Assets and liabilities of C are the assets and liabilities of the incorporated entity
- ▶ Legal form of the separate vehicle indicates that the parties have rights to the net assets of the arrangement

▶ Analysis:

- ▶ Joint venture or Joint operation?

Classification of a joint arrangement

Examples of contractual terms

	Joint Operations	Joint Ventures
Assets	• Share all interests in the assets in a specified proportion • Hold assets of the arrangement as tenants in common in a specified proportion • Have rights to all of the economic benefits generated by the assets	Do not have interests (i.e., no rights, title, or ownership) in the assets of the arrangement
Liabilities	• Share all liabilities, obligations, costs and expenses in a specified proportion • Have liabilities for claims raised by third parties or to customers of the arrangement	• Are not liable for the debts and obligations of the arrangement • Liabilities to the arrangement do not exceed the parties' investment in the arrangement • Creditors do not have any recourse against any party in for debts or obligations

Classification of a joint arrangement

Contractual terms - Example

(Continued)

- ▶ Fact pattern:
 - ▶ A and B modify the features of C through their contractual arrangement so that each has an interest in the assets of C and each is liable for the liabilities of C in a specified proportion

- ▶ Analysis:
 - ▶ Joint venture or Joint operation?

Classification of a joint arrangement

Facts and circumstances

- ▶ Facts and circumstances might indicate a joint operation if they result in the parties having:
 - ▶ Rights to the assets
 - ▶ Obligations for the liabilities

- ▶ This may happen when there is:
 - ▶ Restrictions on customers
 - ▶ Commitments to purchase all the output produced
 - ▶ Expectations to fund losses by venturers
 - ▶ Venturers continuously settle liabilities of the arrangement
 - ▶ Designed to operate at breakeven
 - ▶ Consider purpose and design
 - ▶ Commitment upon default or guarantee is not determinative of being a joint operation

Classification of a joint arrangement

Facts and circumstances - Example

(Continued)

- ▶ Fact pattern:
 - ▶ Neither the legal form or contractual arrangement provide rights to assets and liabilities of the arrangement to the venturers; however
 - ▶ A and B agreed to purchase all the output produced by C in a ratio of 50:50
 - ▶ C cannot sell any of the output to third parties, unless this is approved by A and B (expected to be uncommon)
 - ▶ Price of the output sold is designed to cover expenses incurred by C (intended to operate at break-even level)

Example - Telecom

Fact pattern:

- ▶ A & B establish New Co.
- ▶ Transfer all tower equipment to New Co.
- ▶ A & B have direct rights to assets/liabilities based on their proportionate shareholding
- ▶ All New Co's decisions are unanimously made by A & B

Ind AS 111

Joint Operation because A & B have direct rights to the assets/liabilities

Variation in the Example

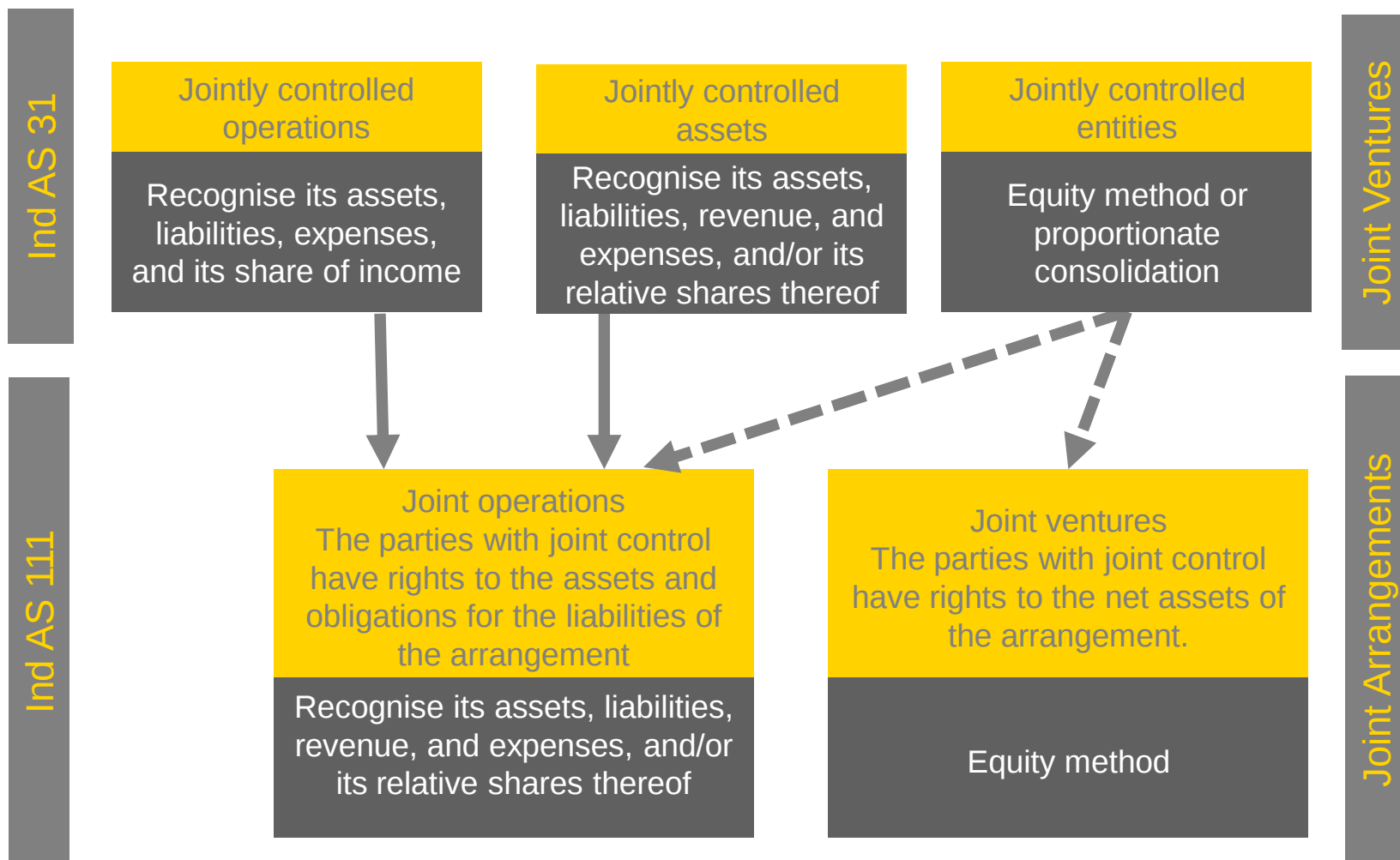
- ▶ A & B do not have direct rights to assets / liabilities of New Co. based on their proportionate shareholding
- ▶ Network capacity will be shared by A & B only.
- ▶ Operated at breakeven level

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Joint operations or Joint venture?

Accounting treatment

Accounting treatment



Accounting for joint operations

- ▶ For a joint operation, the joint operator recognises its:

Assets
(including its share of
jointly held assets)

Liabilities
(including its share of
jointly incurred liabilities)

Revenue
from the sale of its share of
the output arising from the
joint operation

Share of the revenue from
the sale of the output
obtained from the joint
operation

Expenses
(including its share of jointly
incurred expenses)

- ▶ The recognition and measurement (including impairment considerations) for each of these items shall be done in accordance with the applicable Ind ASs

Accounting treatment

Proportionate consolidation vs. joint operation

- ▶ When is accounting for a joint operation the same as ‘proportionate consolidation’?
 - ▶ Equal rights to all assets all liabilities – probably same
 - ▶ Rights to a specified percentage of certain assets and differing rights (and percentages) to other assets, and different obligations for various liabilities – likely to be a difference
 - ▶ Nature of assets and liabilities might change
 - ▶ Assets - same nature as recognised by joint operator OR (for example) reimbursement right?
 - ▶ Liabilities - same nature as recognised by joint operator OR (for example) cash due to joint operation?

Accounting treatment

Joint Operation Example

Fact pattern:

- ▶ D & E establish New Co. (F)
- ▶ The legal form of the separate vehicle does not confer separation between the parties
- ▶ D and E each own 50% of the equity (e.g., shares) in F. However, as per the contractual terms of the joint arrangement:
 - ▶ D has the rights to all of Building No. 1 and the obligation to pay all the third party debt in F.
 - ▶ D and E have rights to all other assets in F, and obligations for all other liabilities in F in proportion to their equity interests (i.e., 50%)

Accounting treatment

Joint Operation Example (continued)

F's balance sheet is as follows (in CU's):

Liabilities and Equity		Assets	
Debt	120	Cash	20
Employee obligation	50	Building 1	120
Equity	70	Building 2	100
	240		240

Under Ind AS 111, D would record the following in its financial statements. This likely will differ from the amounts recorded using proportionate consolidation.

Liabilities and Equity		Assets	
Debt	120	Cash	10
Employee obligation	25	Building 1	120
Equity	35	Building 2	50
	180		180

Accounting treatment

Joint Operation- Determining the relevant Ind AS

Joint operators are required to recognise their rights to assets and their obligations for liabilities in accordance with the relevant Ind AS:

A Joint operator will need to carefully analyse the nature of its rights to assets when determining the appropriate accounting.

For example, a Joint operator would recognise its share of an asset in accordance with Ind AS 16 Plant, Property and Equipment, or Ind AS 38 Intangible Assets, as applicable. When the contractual terms of the joint operation provide a joint operator with a right to use an asset, not a share of the asset itself, the Joint operator would consider determining Whether the Arrangement Contains a Lease in accordance with Ind AS 17.

Accounting for joint ventures- Equity Method

- ▶ Ind AS 111 requires the equity method
- ▶ The application of the equity method continues to be covered in Ind AS 28, however it has below exemptions:
 - ▶ if the entity is a parent that is exempt from preparing CFSs by the scope exception in Ind AS 110, or
 - ▶ When an investment in an associate or a joint venture, is held by, or is held indirectly through, an entity that is a venture capital organisation, or a mutual fund, unit trust and similar entities including investment-linked insurance funds, the entity may elect to measure investments in those associates and joint ventures at fair value through profit or loss in accordance with Ind AS 109.

Disposal of Joint Arrangement

- ▶ Disposal of interest in a joint operation

When an entity disposes of its interest in a joint operation, it ceases to account for the rights to assets and obligations for liabilities, and recognises any gain or loss as of the disposal date.

- ▶ Disposal of interest in a joint venture

When an entity disposes of its interest in a joint venture, it ceases to use the equity method as of that date. It also de-recognises its interest and recognises any gain or loss upon sale.

In both the cases, an entity is not required to restate its financial statements as if it never held the interest in the disposed joint operation / joint venture

Continuous reassessment

Continuous reassessment

- ▶ Accounting for arrangements pre-Ind AS 111 changed mostly in line with changes in ownership interest or changes in contractual arrangements
- ▶ Due to revised definition of control, management also needs to reassess upon changes in facts and circumstances, in addition to the above, for example:
 - ▶ Changes in how activities are directed
 - ▶ Changes in legal form
 - ▶ Changes in other facts and circumstances (such as changes in how the output of the joint operation is sold or how liabilities of the operation are settled)
- ▶ Reassessment required even if steps are predetermined

Disclosures

Disclosures

- ▶ No disclosure requirements in Ind AS 111 in relation to joint arrangements
- ▶ Ind AS 112 combines all disclosure requirements for interests in other entities
- ▶ Detailed disclosures will be discussed in Ind AS 112.

Attention: Ind AS 112 increases the disclosure requirements.

Examples

Example – Manufacturing & distribution

Fact pattern

- ▶ A and B enter into a contract to manufacture and distribute a product in a framework agreement
- ▶ Manufacturing activity:
 - ▶ Separate vehicle (M)
 - ▶ M's legal form causes separation between A and B and M (assets and liabilities of M are its own)
 - ▶ A and B committed to purchasing all of the whole production in accordance with their ownership in M
 - ▶ A and B subsequently sell the product to another joint arrangement, established exclusively for distribution
 - ▶ A and B do not have rights to the assets or obligations for the liabilities relating to the manufacturing activity

Example – Manufacturing & distribution

Fact pattern

- ▶ Distribution activity:
 - ▶ Separate vehicle (D)
 - ▶ D's legal form causes separation between A and B and D (assets and liabilities of D are its own)
 - ▶ D orders its requirements for the product from A and B according to the needs of the different markets where the distribution arrangement sells the product
 - ▶ A and B do not have rights to the assets and obligations for the liabilities relating to the distribution activity

Example – Manufacturing & distribution

Fact pattern

- ▶ Framework agreement also establishes:
 - ▶ M will produce product to meet the distribution requirements of A and B;
 - ▶ M will sell product to A and B at a price that covers all production costs incurred
 - ▶ A and B sell the product to D at a price agreed by A and B
 - ▶ Any cash shortages incurred by M will be financed by A and B in accordance with their ownership interests in M

Example – Manufacturing & distribution Analysis

	Manufacturing	Distribution
Separate vehicle	Yes – M	Yes – D
Legal form	Confers separation between A and B and separate vehicle M	Confers separation between A and B and separate vehicle D
Contractual terms	Assets and liabilities in M are <u>not</u> A and B's assets and liabilities	Assets and liabilities in D are <u>not</u> A and B's assets and liabilities
Other facts and circumstances	• A and B purchase all of the production, and therefore all the economic benefits of M • Exclusive dependence of M on A and B for cash flows (sale of product and funding) indicate A and B have an obligation for the liabilities of M	None that indicate that A and B have rights to substantially all the economic benefits of the assets relating to D, or obligations for the liabilities relating to D
Conclusion		

Example – Manufacturing & distribution Analysis

	Manufacturing	Distribution
Separate vehicle	Yes – M	Yes – D
Legal form	Confers separation between A and B and separate vehicle M	Confers separation between A and B and separate vehicle D
Contractual terms	Assets and liabilities in M are <u>not</u> A and B's assets and liabilities	Assets and liabilities in D are <u>not</u> A and B's assets and liabilities
Other facts and circumstances	• A and B purchase all of the production, and therefore all the economic benefits of M • Exclusive dependence of M on A and B for cash flows (sale of product and funding) indicate A and B have an obligation for the liabilities of M	None that indicate that A and B have rights to substantially all the economic benefits of the assets relating to D, or obligations for the liabilities relating to D
Conclusion	Joint operation	Joint Venture

Example – Manufacturing & distribution

Variation

- ▶ Fact pattern
 - ▶ M also distributes product to other customers
 - ▶ M also sells product directly to the D
 - ▶ No fixed proportion of the production of M is committed to be purchased by, or sold to, D
- ▶ Analysis
 - ▶ Manufacturing: changes to joint venture
 - ▶ M has own customers and own distribution
 - ▶ M has inventory and credit risk
 - ▶ M not dependent on A and B
 - ▶ Distribution: remains joint venture

Difference between Ind AS111 and AS 27

Difference – Ind AS 111 and AS 27

Basis	AS 27	Ind AS 111
Term	•A joint venture is an entity or asset or operation that is subject to contractually established joint control	•Similar to i-GAAP, however, the term 'joint arrangement' is used instead of the 'joint venture'
Jointly controlled entities (JCE) / joint venture (JV) / collaborative arrangements	•Three broad types of joint ventures: • jointly controlled operations • jointly controlled assets • jointly controlled entities	•Joint arrangements are either joint operations or joint ventures. •Joint arrangement not structured through a separate vehicle is a joint operation.
JCEs (consolidated financial statements)	•Jointly controlled entities are accounted for by proportionate consolidation in the CFS	•Joint ventures (i.e.JCEs) are generally accounted for using equity method of accounting.

Difference – Ind AS 111 and AS 27

Basis	AS 27	Ind AS 111
Uniform accounting policies	•Accounting policies must be uniform to those of its venturer, unless impracticable.	•Similar to Indian GAAP except that no impracticability exception exists.
Reporting period	•Reporting dates must be the same •If impracticable, the difference in dates cannot exceed six months •Adjustments are made for the effects of significant transactions or other events that occur between the two dates.	•Similar to Indian GAAP except that the difference in dates cannot be more than three months.

Thank you