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Alan Teixeira
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International Accounting Standards Board
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London
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Exposure Draft ED 9 *Joint Arrangements*

Dear Mr Teixeira,

We are pleased to comment on Exposure Draft ED 9 *Joint Arrangements* (referred to as 'ED 9' or 'the proposed Standard').

Deloitte continues to support the convergence efforts of the world's national accounting standard-setters and the IASB with the objective of developing a set of high-quality global accounting standards which command wide acceptance and support. Whilst we support this process, we have reservations about how the IASB continues to approach its 'short-term convergence' agenda, of which ED 9 is a part.

Part of the IASB's strategy with respect to its short-term convergence agenda is to identify what the Board concludes to be the highest quality solution available from the current population of accounting standards and to move to that standard. We support this approach. However, in ED 9, the IASB has not demonstrated nor put forward conclusive evidence that the approach chosen, i.e. equity accounting, is the highest quality solution for interests in joint ventures, something which the Board acknowledges in its basis for conclusions to the proposed Standard.

As well as eliminating proportionate consolidation, ED 9 proposes a new approach, focussing on contractual rights and obligations rather than the legal form of arrangements. However, as ED 9 is poorly drafted and the IASB's objectives and its rationale for those objectives are not clearly articulated, the requirements and their application are unclear:

- The requirements in the main body of the proposed Standard cannot be understood without reference to the flowchart in the appendices and the guidance in the Illustrative Examples (the latter do not even form an integral part of the proposed Standard).

- ED 9 proposes that interests in joint operations and joint assets be recognised "in accordance with applicable IFRSs" but does not clarify whether:
  - the 'right of use' or entitlement to 'part' of an asset should give rise to the recognition of a tangible, intangible or other type of asset;
  - the unit of account to be applied when determining which assets and liabilities to recognise;
  - how the proposals interact with the 'lease' concept, and when joint arrangements should be accounted for as leases under IAS 17 *Leases* and not under ED 9. For example, the draft Illustrative Examples illustrate accounting outcomes contrary to those that would result if IAS 17 were applied as 'the applicable IFRS'.
  - how the proposed accounting for joint assets, allowing each venturer to recognise its share of the joint asset, can be reconciled to the IASB's rationale for eliminating proportionate consolidation for arrangements involving legal entities.

As a result, it is difficult to distil ED 9's key principles and understand whether the IASB seeks to modify the existing basis of accounting for joint arrangements in addition to eliminating the proportionate consolidation option in IAS 31.

Conducting activities through a joint venture is a business model different from conducting activities though associates or subsidiaries. The proportionate consolidation approach produces an outcome that differentiates joint venture activities. The IASB appears to acknowledge this in its approach in ED 9, supplementing a requirement to use the equity method with a requirement to disclose information that is considered to be useful for users of the financial statements, including information that would result from the use of a proportionate consolidation accounting methodology. Additionally, it appears that the IASB has predominantly focussed on the balance sheet treatment of joint ventures, and has not necessarily considered whether the equity method presents the most relevant and reliable outcome in the income and cash flow statements.

As such, the proposals in ED 9 cut across the IASB's conceptual framework project and many other projects of the IASB, for example in respect of the unit of account, or whether to apply a "look though" approach in separate financial statements where assets are held in a separate legal entity. It is possible, if these proposals go ahead, that there will be inconsistencies between the ED 9 approach and the outcome of these projects, hence that further changes will be required in this area in a relatively short time-frame. One of the IASB's objectives in proposing the elimination of proportionate consolidation is to reduce differences between IFRS and US GAAP in accounting for interests in joint ventures. We are unsure whether these proposals meet this objective. We understand that:

- US GAAP permits the use of proportionate consolidation in certain industries, hence ED 9 would have the effect of creating IFRS-US GAAP differences for those entities.
- ED 9 would require investments in joint ventures held for sale to be accounted for in accordance with IFRS 5 *Non-current Assets Held for Sale and Discontinued Operations*, whereas US GAAP does not permit 'held-for-sale' classification.
- The disclosure requirements under the proposed Standard are not fully converged with US GAAP.

For the reasons above, we believe that it is best for the IASB not to proceed with the proposals in ED 9 at this time.

As stated, we believe that the IASB should strive for the highest-quality solutions in its convergence program. We would therefore prefer for the IASB and FASB to run a full joint convergence project on the accounting for joint arrangements to determine the highest-quality solution. This project should consider how the concept of 'joint control' interacts with the concepts of 'control' (the subject of the IASB's existing consolidation project) and 'significant influence', and the inter-relationships with the IASB's leasing project, conceptual framework project and extractive activities project.

If the Board does decide to proceed with ED 9 in its current form, our responses to the questions raised in ED 9 set out in the Appendix A and additional drafting comments we have included in Appendix B highlight the following key matters:

- The drafting of the proposed Standard needs to be significantly improved. There is a limited amount of guidance on applying its key concepts, which results in difficulties in determining its scope and intended application.
- The key definitions are unclear and suffer from a certain amount of circularity. For example, it is unclear what 'shared decision-making' means and how it is distinct from 'joint control'.
- The proposals represent a significant shift in accounting for these types of arrangements. The accounting outcomes are heavily dependent on the unit of account adopted when applying its requirements. Without additional clarification and guidance, we are concerned that this could lead to increased subjectivity and judgement in applying the final IFRS
- Additional guidance is required, for example, on changes in ownership interests or in the contractual arrangements and how to account for transactions between parties to an arrangement.
- Care needs to be taken that the proposed Standard is considered in light of other pronouncements and projects that the IASB is currently undertaking, particularly the extractive activities project.
- The disclosure requirements of the proposed Standard should be recast as 'principles' and 'guidance'. Many of the principal disclosures required would be better applied to all types of joint arrangements (rather than just joint ventures as is proposed). Some disclosure requirements are excessive and other useful disclosures are omitted.
- We believe it is necessary for the IASB, by reference to the *Framework*, and considering the income and cash flow statements, to justify why equity accounting is a better accounting approach than proportionate consolidation (or some other approach). Many of the reasons given by the IASB for the elimination of proportionate consolidation can also be levelled at equity accounting.

If you have any questions concerning our comments, please contact Ken Wild in London on +44 (0) 207 007 0907.

Yours sincerely

Ken Wild
Global IFRS Leader

Appendix A – Response to specific questions

Question 1 –Definitions and terminology

The exposure draft proposes that the IFRS should be applied to arrangements in which decisions are shared by the parties to the arrangement. The exposure draft identifies three types of joint arrangement—joint operations, joint assets and joint ventures. A party to an arrangement may have an interest in a joint operation or joint asset, as well as an interest in a joint venture. Joint ventures are subject to joint control (paragraphs 3–6 and 8–20 and Appendix A of the draft IFRS and paragraphs BC16–BC18 of the Basis for Conclusions).

Do you agree with the proposal to change the way joint arrangements are described? If not, why?

We support the IASB's rationale for changing the definitions and terminology for joint arrangements. However, we believe that the terminology used in ED 9 could be improved and clarified.

The key definitions used in the proposed Standard are not clear and suffer from a certain amount of circularity, resulting in difficulties in determining the scope and applying the requirements of the proposed Standard.

The paragraphs that follow outline some of these difficulties and our recommendations to address them.

<u>The critical concepts underlying the proposed Standard are unclear</u>

The proposed Standard does not include explicit definitions of "joint asset", "joint operation" and "joint venture", but merely alludes to these concepts by way of narrative descriptions and examples. Furthermore, it is unclear whether the narrative descriptions in paragraphs 8, 11 and 15 of the proposed Standard are intended to be formal definitions of these terms or merely guidance on the types of arrangements that might fall into each of these categories.

Furthermore, the requirements in the main body of the proposed Standard must be read in conjunction with the flowchart in the appendices and the Illustrative Examples in order to understand the accounting proposed by ED 9. Even then, there are many areas of significant uncertainty in understanding and applying these additional materials.

In fact, the flowchart in the appendices might be seen as contradictory to the main body of the Standard. The flowchart focuses on the existence of a contractual arrangement and then articulates the accounting for the various contractual rights arising under that arrangement. The terms 'joint asset', 'joint operation' and 'joint venture' are superimposed on this basic principle, which creates uncertainty and difficulty in determining the intention of the proposed Standard.

The inclusion of the references to 'joint asset' and 'joint operation' may be seen as superfluous given the underlying principle that an entity accounts for its contractual rights and obligations arising under a joint arrangement, if it is this principle that the IASB seeks to implement with ED 9.

The insertion of the reference to 'in accordance with relevant IFRSs' further clouds this issue as it is unclear whether the existing method of accounting for joint assets and joint operations under IAS 31, i.e. a form of 'proportionate consolidation' of an entity's interest in each asset and liability arising under the joint arrangement, will continue to apply under ED 9's proposals. An alternate argument could be that the reference to 'relevant IFRSs' is intended to result in *other* IFRSs being used to account for joint assets and joint operations – most likely IAS 17 (a lease over a part of an asset) or IAS 38 (a form of right or another type of intangible asset) (this matter is discussed further under 'Concerns surrounding the Illustrative Examples' on page 13). It is therefore necessary that a clear definition of 'contractual arrangement' be specified.

The IASB needs to determine whether a pure focus on contractual rights and obligations is the key objective of ED 9, or whether the objective is to carry over from IAS 31 the existing concepts of 'joint asset' and 'joint operation'. If the IASB intends for the carry over from IAS 31, the proposed Standard needs to be rewritten so as to make this accounting outcome clear. Consequential scope amendments would need to be made to other IFRSs to ensure that multiple IFRSs do not apply to joint arrangements, which may otherwise lead to contradictory accounting outcomes.

Definition of "joint arrangement"

The definition of "joint arrangement" refers to a "contractual arrangement whereby two or more parties undertake an economic activity together and share decision-making relating to that activity".

The definition of "shared decisions" refers to "decisions that require the consent of all of the parties to a joint arrangement".

It is unclear whether the reference to the term "share decision-making" in the definition of a "joint arrangement" is intended to have the same meaning as "shared decisions". If the meaning is intended to be the same, then it would appear that in order to meet the definition of a joint arrangement, all parties to the contractual arrangement would need to consent to the decisions surrounding the joint arrangement.

This may create doubt about whether or not certain contractual arrangements meet the definition of "joint arrangements", such as arrangements where decisions are made by contractual majority. For example, this may occur where several, but not all, parties to a joint arrangement together must agree to effect decisions, but one or more other parties, whilst being able to participate in the decision-making process, are unable to change the outcome of any particular decision.

This issue is amplified in the particular case of joint ventures, where the additional definitions of "venturer" and "joint control" could be read to require the consent of all parties to the joint arrangement, rather than those considered 'venturers'.

We do not believe that these outcomes are the intention of the IASB and we recommend that the definitions be amended to clarify this point. It would also be useful to include guidance or an illustrative example that clearly indicates how parties that meet the definition of a 'venturer' are determined.

The nature of "shared decision-making"

The proposed Standard only applies the concept of "joint control" to joint arrangements, or parts of joint arrangements, that meet the definition of a "joint venture". "Joint operations" and "joint assets" rely solely on a concept of "shared decision-making". However, the proposed Standard does not articulate how this concept is intended to operate.

As a result, it is unclear what types of decisions are intended to be within the ambit of the "shared decision-making" definition. Paragraph 7 of the proposed Standard provides some examples of what is commonly included in a contractual arrangement but they do not appear to relate to sharing of decision-making relating to the activities.

The proposed Standard therefore needs to clarify what "shared decision-making relating to that activity" means, and to what extent the decisions that relate to the activity require the consent of the parties involved and how it is distinct from "joint control". Upon reflection, it may be considered necessary to incorporate some reference to 'financing and operating decisions' into the concept of 'shared decision-making', which may render the distinction from 'joint control' redundant.

Notwithstanding the above comments, in the event that the reference to 'shared decision-making' is retained, we recommend that the proposed Standard clearly articulate the principles that are to be applied in determining whether "shared decision-making" exists in a particular arrangement. The principles should be reinforced with appropriate guidance in order that the principles are easily understood and applied.

Without the clear articulation of the principles to be applied, we expect that constituents are likely to encounter difficulty and uncertainty in applying the existing guidance in practice. The examples below illustrate some of the areas where difficulty and uncertainty may arise. Whilst we do not recommend developing detailed guidance on each of these areas (which would risk a 'rules-based' approach), we believe that the IASB should ensure that the principles and guidance articulated in the final IFRS allow constituents to answer these types of questions:

- When, and if so how, 'dead lock' mechanisms should be taken into account in determining whether or not there is shared decision-making over a joint arrangement;
- Whether shared decision-making should encompass all decisions made in relation to the joint arrangement, or whether it is only intended to apply to specific types of decisions, e.g. operational requirements, cash flow forecasting, personnel appointments, location and composition of administrative and other functions, etc;
- The type and nature of decisions (minor or otherwise) that do not need to be taken into account in assessing whether or not shared decision-making exists and how those decisions are to be distinguished from decisions that are determinative in the assessment of whether or not shared decision-making exists – i.e. is the concept of "strategic" decisions from IAS 31 intended to be maintained under the proposed Standard? We note that paragraphs BC 21-23 of IFRS 3 (March 2004) acknowledges, that following comments from constituents, the Board decided to retain the word strategic in the definition of joint control;
- How contractual arrangements creating the joint arrangement are to be taken into account in determining shared decision-making when those contractual arrangements appoint one of the parties to the arrangement (or an independent party) as the 'operator' of the joint arrangement; and
- Whether the proposed Standard would capture a time-share arrangement where decisions about the asset over which the time-share arrangement exists require consent from all time-share holders in respect of certain specified decisions.

<u>Reference to "business"</u>

The proposed Standard includes references to, and a definition of, a "business" in relation to joint ventures. However, it is unclear why the proposed Standard includes this reference and how it is intended to be considered in light of the requirements of the Standard.

For instance, paragraph 18 of the proposed Standard includes a reference to a 'business'. It is unclear whether this is merely providing an example of a "joint venture" or whether it is implying that for an entity to have an interest in a joint venture, the joint venture must be a business. Paragraph 17 also notes that a "joint venture controls assets, incurs liabilities and expenses and earns revenue" which may be seen as akin to the concept of a 'business'.

This casts doubt on whether 'single asset' entities can qualify as a 'joint venture' if the activities conducted through the entity are not a 'business', e.g. an entity with an interest in a holding company that holds one investment property that is not a business, or a joint arrangement between parties to construct an asset where the construction activities may not meet the definition of a 'business' but the activities are administered through an incorporated entity that is owned by the parties to the arrangement.

Furthermore, paragraph 18 implies that a "business" that is subject to joint control must be classified as a joint venture unless circumstances indicate otherwise. Whilst this statement is qualified by the sentences that follow, we believe this requirement, combined with the commentary in paragraph 17 about the nature of a joint venture, together effectively create a 'rebuttable presumption' that a joint venture must involve the existence of a business and that a joint arrangement over a business would normally be classified as a joint venture.

The 'rebuttable presumption' effectively created by paragraphs 17 and 18, combined with the substance over form approach of the proposed Standard, could result in a number of 'unincorporated' joint arrangements being equity accounted even though the parties to the joint arrangement do not have an interest in a separate legal entity or arrangement.

However, where a joint arrangement is a right to share a percentage of the profits of an asset, it is unclear how this arrangement should be accounted for in accordance with the equity accounting requirements proposed in ED 9. The near-final draft of the revised IFRS 3 *Business Combinations* makes a clear distinction between the purchase of an asset and the purchase of a business, but ED 9 does not deal with this issue in the context of a single asset that is subject to a joint venture arrangement. In particular, it is unclear whether the entire purchase price of the investment in the joint venture entity should be ascribed to the asset, or whether a bargain purchase would lead to the recognition of a gain, following the principles of IFRS 3.

We recommend that:

- The reference to "business" should be removed from the proposed Standard, including the deletion of the definition of "business" from Appendix A;
- The presumption that a business is a joint venture unless circumstances indicate otherwise be deleted from the proposed Standard; and
- If the definition of "business" is not removed as proposed above, the operation of the proposed Standard be clarified in relation to both incorporated and unincorporated joint arrangements whose activities do not meet the definition of a 'business'.

<u>Definition of "joint control"</u>

The definition of "joint control" in the proposed Standard refers to *"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"*.

The definition does not include a reference to "shared decisions". Accordingly, it is unclear whether an arrangement could be characterised as a joint venture on the basis of the *sharing* of the power to govern the financial and operating policies of a venture in situations where the parties to the arrangement are not all required to provide consent to decisions.

We recommend:

- The definition of "joint control" be amended to include a requirement for 'shared decision-making' (this may require the defined term to be "shared decision-making" rather than "shared decisions"); and
- Commentary or guidance be provided to illustrate how the concept of "joint control" is to be determined in practice.

Questions 2 and 3 – Accounting for joint arrangements

The exposure draft proposes:

- ***that the form of the arrangement should not be treated as the most significant factor in determining the accounting.***
- ***that a party to a joint arrangement should recognise its contractual rights and obligations (and the related income and expenses) in accordance with applicable IFRSs.***
- ***that a party should recognise an interest in a joint venture (ie an interest in a share of the outcome generated by the activities of a group of assets and liabilities subject to joint control) using the equity method. Proportionate consolidation would not be permitted.***

Question 2: Do you agree that a party to a joint arrangement should recognise its contractual rights and obligations relating to the arrangement? If so, do you think that the proposals in the exposure draft are consistent with and meet this objective? If not, why? What would be more appropriate?

We have concerns on the practical implications of taking this approach. The principles that are to be applied in meeting the objective are not clearly articulated in the proposed Standard and it is also unclear how the proposals in ED 9 interact with:

- various other projects of the IASB, as commented on generally throughout this letter;
- the concept of 'unit of account', as commented on below; and
- closely-related Standards, particularly its interaction with IAS 27 and IAS 28.

Furthermore, in the event that the proposals in ED 9 are implemented:

- the main body of the final IFRS must clearly articulate the key principles that are to be applied in meeting the objectives of the Standard;
- there is a need for requirements and guidance in many areas that are not addressed in the proposed Standard; and
- the Illustrative Examples need to be expanded and improved to address some concerns presented below.

Further information on each of these concerns is outlined below.

<u>Unit of account</u>

The substance over form approach proposed in ED 9 may in some respects seem premature when considered in the light of the wider projects being undertaken by the IASB. This project is heavily dependent on the notion of 'unit of account' which is currently being debated by the IASB in its conceptual framework, insurance and other projects.

The *Framework for the Preparation and Presentation of Financial Statements* currently lacks guidance on how to account for 'parts' of assets or rights to particular aspects of assets. The proposed Standard in some cases illustrates that parts of assets and liabilities be used as the unit of account.

Other pronouncements, such as IFRIC 4 *Determining Whether an Arrangement contains a Lease*, allude to the issue of unit of account in relation to parts of assets, however they do not provide definitive guidance on how the unit of account is to be determined.

We are concerned that the recognition of parts of assets as the unit of account under the proposed Standard may be difficult to apply in practice and may also set precedent in other areas. For instance, draft Illustrative Example 3 provides an interest in one floor of a building as being a separately accounted for asset on the basis of the combined effect of the joint arrangement agreement and an associated lease arrangement.

The proposed Standard also does not clearly articulate the nature of assets and liabilities that are recognised on application of its requirements, instead referring the reader to "applicable IFRSs". Many IFRSs do not explicitly consider the recognition and measurement of a part of an asset or a shared obligation. Accordingly, the reader is left to determine how items should be treated. For instance, should an undivided interest in a tangible asset be considered a tangible asset in its own right, a right of access/use, a leased asset, some form of intangible asset or something else?

Without more explanation and guidance it is difficult to determine:

- the key principles that are to be applied in meeting the objective of recognising an entity's contractual rights and obligations;
- when agreements and other factors should be considered together in order to delineate a part of an asset as the unit of account for the purposes of the proposed Standard;
- on what bases the unit of account can be delineated, e.g. does it extend to undivided interests in assets, finance and operating leases, time-share arrangements, rights of access for particular time periods, encumbrances and other rights over land, etc; and
- how to determine the nature of the assets and liabilities recognised – for example whether assets are tangible or intangible, some other form of right or obligation and so on. This also applies to the situation mentioned in paragraph 6 relating to a guarantee provided by the shareholder of a limited liability company – would the shareholder need to record the share of the liability guaranteed or simply the guarantee issued?

The proposed Standard, Illustrative Examples and Basis for Conclusions do not state the principles to be applied, nor do they explicitly address the unit of account issue and how the IASB reached its conclusions on this issue.

We recommend that the IASB:

- clearly articulates within the main body of the final IFRS the key principles that are to be applied in meeting the objectives of the Standard;
- carefully explains its rationale around the concept of 'unit of account' in relation to joint arrangements within the scope of the proposed Standard;
- provides additional guidance on how the unit of account is to be determined, including when agreements are to be considered together in making that determination and the parts of assets to be separately accounted for under the proposed Standard; and
- includes guidance in the proposed Standard on how the nature and classification of recognised assets and liabilities is to be determined.

Interaction with IAS 27 and IAS 28

The proposed Standard (like IAS 31 *Interests in Joint Ventures*) is closely related and heavily dependent on both IAS 27 *Consolidated and Separate Financial Statements* and IAS 28 *Investments in Associates* and is also closely linked to the consolidation project and the concepts of 'agent and principal', which are currently being considered by the IASB.

IAS 28 and IAS 31 are predominantly applied from a legal perspective when determining how entities should account for investments in other entities, particularly in separate financial statements prepared following the requirements of paragraph 37 of IAS 27. As a result, it would be rare in the separate financial statements of an entity that the legal form of entities were 'looked through' such that individual assets and liabilities were brought onto the balance sheet of the investee.

The requirements of the proposed Standard produce a different outcome for joint arrangements, according to which, as a result of the contractual and other arrangements around the interest, some (or all) of the individual assets and liabilities of the arrangement would be recognised on the balance sheet of the investor in its separate financial statements. These assets and liabilities would then not be recognised in the separate financial statements of the investee.

The outcomes that result under the proposed Standard and IAS 27 and IAS 28 can therefore in some cases be considered inconsistent. For instance, an employee benefit share trust that is controlled by an entity would not generally result in 'collapsing' of the trust into the parent in the parent's separate financial statements, even though the substance of the arrangement (considering all the contractual arrangements between the company, its employees and the trust together) may suggest otherwise.

We recommend that the IASB considers this apparent inconsistency and provide additional commentary and guidance. Alternatively, the IASB could consider broadening its consolidation project to encompass accounting for arrangements over which the entity has joint control or significant influence.

<u>Areas where more guidance is required</u>

Changes in ownership interests in joint ventures without losing joint control

The proposed Standard does not provide sufficient guidance surrounding the accounting for changes in ownership interests in joint ventures.

There is one sentence included in paragraph 32 of the proposed Standard dealing with the treatment of amounts previously recognised in other comprehensive income where there has been a reduction in the ownership interest in a joint venture.

However, there is no guidance on the following matters:

- how any gain/loss arising from the partial disposal of an interest is to be measured, classified and presented in the financial statements;
- how changes in ownership interests are to be accounted for, particularly as a change in ownership interest will increase and decrease each investor's entitlement to the contributed capital, reserves and retained earnings of the investee;
- how changes in ownership interests that do not relate to a purchase or sale by the investor are to be accounted for, e.g. the introduction of a new party to the joint arrangement by way of that party contributing cash into the joint venture;
- how the proposed Standard would be applied in light of the revised IFRS 3 *Business Combinations* and IAS 27 *Consolidated and Separate Financial Statements*, particularly:
    - the requirement to treat transactions between controlling and non-controlling interests as equity transactions – is this approach intended to apply to entities under joint control as well?
    - the accounting treatment to be applied where an investment in an entity previously accounted for under IAS 39 becomes a joint venture that is subsequently accounted for under the equity method in accordance with the proposed Standard – is the fair value of investment at the time joint control is obtained to be considered the 'cost' for initial application of the equity method? Furthermore, should any gains and losses in an available-for-sale reserve in respect of the prior interest be recycled to the income statement on gaining joint control?

Whilst we recognise that many of these issues also arise in relation to equity accounting for associates under IAS 28, we recommend that the IASB develops requirements in relation to the above matters.

Further, paragraph 6 of ED 9 indicates that a contract, such as a guarantee contract, provided by the shareholder of a limited liability company can negate the effect of the limited liability for that shareholder. There is however no guidance on whether and how such a situation would impact the determination of whether a joint arrangement exists. More generally, we do not understand how the fact that the limited liability is negated impacts the determination of whether or not a joint arrangement was created.

Transactions between parties to a joint venture

We acknowledge that ED 9 proposes to withdraw SIC-13 *Jointly Controlled Entities- Non-Monetary Contributions by Venturers* and to replace it with a general reference to the equity method adopted in IAS 28.

However, we believe that this approach is not sufficient for the following reasons:

- a joint venture is subject to joint control, whereas an associate is subject to significant influence. Transfers of assets between an investor and a joint venture result in a move between *control* and *joint control* over the transferred assets (or vice versa). In our view, the difference between control and joint control is more subtle than the difference between control and significant influence and therefore specific guidance around the types of transactions contemplated in SIC-13 is useful; and
- the rationale behind SIC-13 was developed by reference to the requirements of IAS 31 not IAS 28 and the requirements do not appear to have been expressly reconsidered by the IASB in developing ED 9.

Other matters

The proposed Standard does not deal with accounting for the following:

- how to account for changes in the contractual arrangements surrounding a joint arrangement;
- changes in ownership interests under contractual arrangements, particularly in relation to joint assets;
- the acquisition and disposal of interests in joint operations and joint assets; and
- accounting by the joint venture entity for contributions of assets at formation, i.e. should the joint venture recognise the contributed assets at fair value or on a ‘carryover’ basis? US GAAP has some limited guidance in this area and we recommend that the IASB addresses this accounting as part of its convergence project.

The Draft Illustrative Examples provide limited guidance that touch on some of these areas. However, we have concerns about the method of accounting *implied* by those examples (some of these concerns are outlined in the next section below). We would strongly prefer that clearly articulated principles be included in the proposed Standard on these matters.

However, appropriate exemptions and/or modifications for assets and liabilities related to extractive activities would need to be incorporated so as not to make scope exemptions in various Standards redundant, or to ‘second guess’ the IASB’s extractive activities project.

Guidance on appropriate accounting should be extended to all parties to a joint arrangement

Unlike the existing IAS 31, the proposed Standard does not contain any guidance on how parties to joint arrangements that do not share in joint control (in the case of joint ventures) or shared decision-making (in the case of joint assets and joint operations) should account for their interests in the joint arrangement.

In our experience, this has been an area of significant difficulty under the existing IAS 31, notwithstanding the guidance in paragraph 51 of that Standard.

There is currently a lot of uncertainty as to how parties to jointly controlled operations and jointly controlled assets (as defined in IAS 31) that do not share in 'joint control' should account for their interest in those joint ventures. Because the existing IAS 31 has a stronger emphasis on the 'legal form' of joint venture arrangements, the wording of paragraph 51 is commonly only applied to joint ventures where the joint venture is operated through an incorporated joint venture and so each investor has a legal 'investment' in the form of shares or other ownership interest.

Accordingly, there is effectively no guidance on how non-jointly controlling parties to a jointly controlled operation or jointly controlled asset should account for their interests in the unincorporated joint venture. From our experience, some entities account for their interest as a financial asset, others as an intangible asset and others as an 'undivided interest' in the underlying assets. The accounting outcome often depends on the exact facts and circumstances surrounding the joint venture arrangement.

These issues are further complicated under the proposals in ED 9. Because ED 9 focuses on the contractual terms around the joint arrangement rather than the legal form, the issue of how parties that do not participate in joint control or shared decision-making (depending on the nature of the joint arrangement) should account for their interests takes on additional importance, particularly when one joint arrangement can be split into 'parts' and each part can be accounted for differently.

For example, in the case of a joint asset, it is unclear in conceptual terms why parties that have joint ownership over that asset can potentially have different accounting outcomes depending on whether or not they participate in shared decision-making. The absence of shared decision-making by a particular party may be due to a contractual majority requirement for decisions whereby the party is fully entitled to vote, but cannot influence the outcome of any vote due to a relatively small interest in the joint arrangement.

A party to such an arrangement that does not participate in shared decision-making will nevertheless meet many of the factors outlined in paragraphs 11 to 14 of ED 9, including some or all of the factors included in paragraph 13. Generally, the party will have legal and beneficial ownership of the proportion of the assets to which it is entitled, and commonly the party's share of each asset will be separately recognised for taxation purposes as well.

Similar arguments can be made in respect of joint operations and in relation to parties to *unincorporated* joint ventures that do not share in joint control and to joint arrangements that are bifurcated into various types of joint arrangements.

This issue is also closely aligned with our comments above on the 'unit of account'.

We recommend that the IASB consider providing guidance on this matter in the final IFRS.

Concerns surrounding the Illustrative Examples

The Draft Illustrative Examples accompanying ED 9 contain a number of examples that are useful in understanding and applying its requirements, particularly in light of our earlier comments regarding the difficulty in applying the core concepts, definitions and terminology in the main body of the proposed Standard due to poor drafting.

However, we have some concern about a number of examples in the Draft Illustrative Examples, particularly relating to the extractive industries where past and current practice on some of the accounting policies illustrated tend to be diverse. Whilst the clarification in the proposed Standard is in some regards welcome, we are concerned that many of the issues illustrated cut across the IASB's project on extractive activities hence caution is warranted in the way that the examples are worded and presented.

In addition, and as noted earlier in this submission, it would be helpful that where the accounting approaches dealt with in the examples illustrated a principle of the proposed Standard, for these principles to be clearly stated and for the basis for conclusions to outline the IASB's rationale for adopting those principles.

Example 2 – Joint interest in a jet aircraft

Example 2 outlines the treatment of an arrangement whereby five parties jointly buy a jet aircraft and enter into an agreement whereby each party has the right to use the aircraft for its own purposes some days each year. The example goes on to suggest that each party recognises its rights to the aircraft in accordance with applicable IFRSs and that in the event that the aircraft is held in a separate legal entity, that the joint venture entity would recognise an aircraft asset that excludes the rights of use transferred to the parties (the example is unclear about the nature of the asset that would be recognised by the joint venture).

Whilst we understand the rationale behind the analysis provided in this example, we suggest that an alternate and equally valid approach would be for the parties to account for the arrangement in accordance with IAS 17 *Leases*. Accordingly, this example serves to illustrate the potential conflict between the proposals in ED 9 and IAS 17 discussed earlier in this letter[1].

Example 5 – Mining unitisation arrangement

Example 5 illustrates a mining unitisation arrangement whereby entities which each have rights to extract minerals from adjacent areas enter into a contract to combine their operations into one combined area for the purpose of sharing costs. Each party retains legal ownership of the extractive rights for their respective areas and the participation percentages are adjusted on the basis of the findings of an independent study of reserves (sometimes called a 'redetermination').

In this instance, the joint arrangement is considered to involve joint assets, meaning that each party recognises its respective interest in the mineral rights, production equipment, minerals extracted, liabilities incurred, decommissioning liabilities and financing of the operations. We again note that the example is not clear as to the nature of the asset to be recognised.

In the event that there is no redetermination process, the example states that whilst the arrangement involves joint assets, the initial setup of the unitisation arrangement is considered the exchange by each party of its interest in its original mineral rights for a percentage of the mineral rights in the combined area.

Under this view of unitisation arrangements, it would be expected that a sale transaction would be recognised, leading to the recognition of a gain or loss on the initial set up of the unitisation arrangement.

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1 This matter could be resolved by amending IAS 17 to include a scope exemption for arrangements subject to the proposed Standard, which would then result in the accounting provided in the illustration being applied.

Our experience is that this approach is not always followed by entities in relation to unitisation arrangements, particularly where they involve the exploration and evaluation or early development phases, where the fair values of the various assets involved in the unitisation can be difficult to determine.

The example also does not deal with the common situation whereby the unitisation arrangement undergoes a number of redeterminations before the final percentages in the overall field are locked in by way of a final determination. The implied guidance in this Illustrative Example could lead to the recognition of a gain or loss at the time of final redetermination, as this could be considered the sale of the underlying interest in exchange for a new interest in the combined field at that time.

Example 6 – Oil and gas 'farm-in' arrangement

Example 6 deals with a typical 'farm-in' arrangement whereby two parties each earn a 25% working interest in an exploration field by spending CU2 million. The arrangement is considered to involve joint assets with each entity recognising their interest in the exploration assets and operating costs, and any financing of the operations.

More importantly, the arrangement is also characterised as a cost-sharing and risk-sharing arrangement whereby the entity farming-out is selling an interest in exploration assets and the entities farming-in are buying an interest in the exploration assets. Explicit guidance is provided that at the time of the agreement, the entity farming-out recognises a gain or loss on disposal of exploration assets in accordance with applicable IFRSs.

The issue of how to account for farm-ins and farm-outs under IFRS is an area of considerable conjecture. As a large number of these types of arrangements commonly arise during the exploration and evaluation phase of the extractive activity operations, the predominant applicable standard is IFRS 6 *Exploration for and Evaluation of Mineral Resources*.

In some jurisdictions, it is common practice to adopt a 'capitalisation approach' for exploration and evaluation expenditures. Under this approach, an asset is created in relation to each area of interest where activities in the 'area of interest' have not at reporting date reached a stage which permits a reasonable assessment of the existence or otherwise of economically recoverable reserves.

Because of this 'capitalise if unsure' approach, the exploration and evaluation asset is viewed as a cost accumulation of all expenditure in relation to the area of interest. If the entity then farms-out an interest in the overall area of interest, the following approaches are commonly adopted:

- if cash is received as a result of the farm-out arrangement, the amounts received are used to reduce the asset as it can be seen as a 'recovery of cost';
- if cash is not received (such as a 'free carry' arrangement for a period of time or for an agreed amount), often no entries are made and the accumulated costs are carried forward as the cost of the entity's interest; and
- in some cases, the asset may be tested for impairment if the carrying amount of the asset is higher than the implied value of the farm-out arrangement, i.e. the arrangement is considered to trigger the modified impairment indicator approach dictated by IFRS 6 – although under a pure 'cost accumulation' approach this is not always followed so long as the other requirements of IFRS 6 are met, i.e. none of the modified indicators of impairment are triggered.

Similarly, the entity farming-in to the area of interest might also adopt a 'cost accumulation' approach and recognise an exploration and evaluation asset as the amounts are spent, rather than as an upfront purchase transaction with an associated liability. This approach is often justified by reference to the requirements of IFRS 6 and the optionality implied in the farm-in arrangement, i.e. most of these arrangements permit the entity farming-in to choose not to expend the full committed amount and thereby relinquish its interest in the tenement.

Many entities involved in the extractive industries strongly prefer a ‘cost recovery/ accumulation’ approach rather than a ‘sale and purchase’ approach with farm-ins and farm-outs over exploration and evaluation interests. They argue that the asset is uncertain and that under the ‘cost accumulation’ approach it would be misleading to show a gain or loss as a result of a farm-out arrangement when the arrangement is in substance a means of sharing costs and spreading risk.

In light of the above, we recommend that the Illustrative Examples do not attempt to ‘second guess’ the outcome of the IASB extractive activities project by effectively suggesting a particular form of accounting in relation to the examples in this industry. If the examples are retained in the final IFRS we recommend that they be redrafted in a way that indicates that the methodology adopted is the entity’s chosen accounting policy, so as not to imply that the methodology illustrated is the only accounting approach that might be adopted.

Question 3: Do you agree that proportionate consolidation should be eliminated, bearing in mind that a party would recognise assets, liabilities, income and expenses if it has contractual rights and obligations relating to individual assets and liabilities of a joint arrangement? If not, why?

We appreciate that the proposals in ED 9 are consistent with the IASB’s desire, which we support, to eliminate accounting policy options that are currently available under IFRS.

However, as discussed in our covering letter, we are concerned that the IASB has not sufficiently considered and developed its rationale for the proposal to eliminate proportionate consolidation and its choice of retaining the equity method of accounting.

The existing requirements of IAS 31 *Interests in Joint Ventures* are considered by many to be a pragmatic solution to the difficult question of accounting for interests in entities where the investor is not a passive insignificant investor, but is also neither a controlling shareholder.

The argument that proportionate consolidation is inconsistent with the *Framework*, without a true and thorough analysis of accounting for joint arrangements, in our view, leaves the IASB open to criticism that it has proposed a solution only for the sake of US GAAP convergence. Indeed, because US GAAP itself permits the use of proportionate consolidation in some circumstances, the proposals in ED 9 may even be defective in achieving this objective, effectively creating GAAP-to-GAAP differences that did not previously exist.

<u>The IASB has not explained why equity accounting is a better approach</u>

By its own admission, the IASB has not considered the merit of the equity method in developing its proposals in ED 9[2]. Instead, the IASB has focussed on the “fundamental inconsistency with the *Framework*” that proportionate consolidation is considered to represent[3].

Equity accounting is considered by many to effectively be a ‘one-line consolidation’[4]. Accordingly, this same criticism could be levelled at the use of the equity method as it in substance largely adopts a proportionate consolidation approach, but presents the outcome as a single amount in the balance sheet and income statement. In doing so, the equity method effectively conceals the detail that proportionate consolidation provides and necessitates the disclosure of detailed financial information used to perform equity accounting so that users are provided with useful and relevant information.

For this reason, we have some sympathy with the proponents of proportionate consolidation who argue that proportionate consolidation is a practical way in which to present a venturer’s

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[2] Draft Basis for Conclusions, paragraph BC14.
[3] ibid, paragraph BC12.
[4] This is alluded to in IAS 27 *Consolidated and Separate Financial Statements*, paragraph 20.

interest in a joint venture[5]. Proportionate consolidation does produce financial statements that present a complete picture of an entity's operations, without regard to the legal form through which those operations are conducted.

The IASB's argument that proportionate consolidation is inconsistent with the *Framework* appears to have predominantly focussed on the balance sheet treatment of joint ventures, rather than also considering whether the equity method presents the most relevant and reliable outcome in both the income statement and cash flow statement. The *Framework* indicates that financial statements should provide a true representation of performance of the enterprise, i.e. its results and cash flows. We question whether this aspect of the *Framework* has been fully considered when proposing that the equity method be used to account for joint ventures.

In conclusion, because both proportionate consolidation and the equity method are difficult to support by reference to the current *Framework*, we question whether the arbitrary elimination of proportionate consolidation without a complete analysis of this issue is appropriate.

<u>Accounting for joint assets is akin to proportionate consolidation</u>

We also note that the IASB's proposals in ED 9 in accounting for 'joint assets' could, in some respects, also be considered to be contradictory to the position taken in relation to proportionate consolidation. The predominant reason for the IASB's rejection of proportionate consolidation as inconsistent with the *Framework* is that it presents assets that the entity does not control on the entity's balance sheet.

Again, the same criticism could be levied at the inclusion of a proportionate share or component of an asset on an entity's balance sheet as the asset *as a whole* is not under the control of the investor. This issue is obviously closely linked to our earlier observations regarding the appropriate determination of the unit of account when accounting for these types of arrangement. However, from a commercial perspective, it can be difficult to argue that the proposed accounting for joint assets is materially different from proportionate consolidation, except based on a theoretical argument that relies on the *Framework,* which is itself outdated and excludes contemplation of such arrangements.

<u>The differences between equity accounting and proportionate consolidation have not been fully explored</u>

Because the IASB's approach to developing the proposals in ED 9 has been to focus on eliminating proportionate consolidation, the IASB has not fully explored the differences between the equity method and proportionate consolidation. We would recommend that the IASB consider these differences to determine which approach is conceptually superior. If the IASB decided to proceed with the proposal to eliminate proportionate consolidation, it must also ensure that the outcomes under the mandatory application of the equity method produce an outcome that is superior to allowing entities the existing choice between the equity method and proportionate consolidation.

Some of the critical differences are discussed briefly below.

Capitalisation of borrowing costs

Where proportionate consolidation is applied, it is possible for an entity to capitalise borrowing costs into the cost of assets that are proportionately consolidated, whereas under the equity method it is generally held that capitalisation of borrowing costs into the cost of the investment is prohibited. To require capitalisation in relation to 'controlled' assets, but not those that are subject to joint control through a joint venture creates differences based on legal form even though from a commercial perspective the funding of the construction of an asset directly as apposed to through a joint venture may be seen to be substantially similar to each other.

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5 Basis for Conclusions, paragraph BC12.

If the IASB ultimately decides to make use of equity accounting for joint ventures, we would like the IASB to consider whether our understanding is correct, particularly in light of the recent amendments to IAS 23 *Borrowing Costs* to require the capitalisation of borrowing costs.

Other differences

Other differences between proportionate consolidation and the equity method that should be considered include:

- The suspension of the equity method when the equity accounted carrying amount of the investment is reduced to zero, whereas these losses would be included in consolidated profit or loss under proportionate consolidation;
- The inclusion of long-term interests that in substance form part of the investor's net investment in the associate in the equity-accounted carrying amount of the investment, which might otherwise be eliminated if proportionate consolidation were adopted;
- The current and deferred taxes associated with the investee's assets, liabilities, transactions and events are included 'above the line' under the equity method rather than being aggregated with the overall income tax expense as is the case with proportionate consolidation;
- The elimination of transactions between the investor and investee are often limited to unrealised profits only in the case of the equity method, whereas under proportionate consolidation, all transactions are eliminated to the extent of the proportionate ownership interest in the joint venture
- When conducting impairment testing, the allocation of an impairment loss to assets and liabilities of a cash-generating unit can be different depending upon whether the joint venture is accounted for using proportionate consolidation or the equity method. In addition, under the equity method, an impairment loss allocated to goodwill can effectively be reversed, which would not be the case under proportionate consolidation; and
- The elimination of a venturer's treasury shares held by joint ventures may also result in different outcomes depending upon whether the venturer uses equity accounting or proportionate consolidation to account for the joint ventures.

<u>The IASB has not considered other options</u>

By eliminating one existing option under IFRS without a thorough analysis of the issue, the IASB has not considered other alternative accounting treatments that might be adopted in respect of joint ventures.

We set out below some observations on other possible approaches that might be adopted, although we are not proposing that the methods of accounting illustrated are necessarily appropriate for joint ventures. However, it does serve to illustrate that the IASB's analysis of this issue has been superficial.

Fair value methodology

The IASB has determined that it is appropriate to adopt a fair value measurement basis for investments in entities where the investor lacks control, joint control or significant influence. This approach effectively includes the investee's intangible assets, goodwill and other assets on the balance sheet of the investor, revalued to fair value on an ongoing basis.

By contrast, even though an entity does not control a joint venture, it is required to apply consolidation techniques to some extent in accounting for its interest in the joint venture regardless of whether the proportionate consolidation or the equity method is used. These approaches rely on consolidation concepts which, combined with the requirements of other

IFRSs, effectively prohibit the use of the fair value method to measure the investment in the entity.

We consider that it is conceptually difficult to reconcile these different accounting approaches between investments where the investor has joint control and investments where the investor lacks such joint control.

A hybrid approach

As noted above, the IASB appears to have focussed on the balance sheet impact when concluding that proportionate consolidation is inconsistent with the *Framework*, without considering the impact on the other financial statements.

It might be possible to take an 'equity accounting' approach to the recognition of an interest in the balance sheet, but a 'proportionate consolidation' approach to the recognition of income and expenses. This approach might allow for performance information about business activities conducted through joint ventures to be aggregated with like items in the income statement, rather than aggregating all amounts (including income taxes and significant items) into one amount on the income statement. However, in the balance sheet, the 'investment' in the joint venture could be presented as a single line item, differentiating jointly controlled assets and liabilities from the other assets and liabilities of the entity.

Separate presentation

A further alternative could be to expand the IASB's existing projects on the reporting entity and financial statement presentation to address the issue of accounting for joint ventures in more detail. The option of 'another form' of financial statement, or section of the financial statements being developed, that separately presents the effects of joint ventures (and associates) could be explored.

Questions 4–6 – Disclosure

The exposure draft proposes:

- ***to require an entity to describe the nature of operations it conducts through joint arrangements (paragraph 36 of the draft IFRS and paragraph BC22 of the Basis for Conclusions).***
- ***to align the disclosures required for joint ventures with those required for associates in IAS 28 Investments in Associates (paragraphs 39–41 of the draft IFRS and paragraph BC23 of the Basis for Conclusions).***
- ***to require the disclosure of summarised financial information for each individually material joint venture and in total for all other joint ventures (paragraph 39(b) of the draft IFRS and paragraph BC13 of the Basis for Conclusions).***
- ***as consequential amendments to IAS 27 Consolidated and Separate Financial Statements and IAS 28, to require disclosure of a list and description of significant subsidiaries and associates. Those disclosure requirements were deleted in 2003 as part of the Improvements project. However, the Board understands from users that such disclosures are useful.***
- ***as a consequential amendment to IAS 28, to require disclosure of current and non-current assets and current and non-current liabilities of an entity's associates. The proposed IFRS would require disclosure of current and non-current amounts, whereas IAS 28 currently requires disclosure of total assets and total liabilities.***

Question 4: Do you agree with the disclosures proposed for this draft IFRS? If not, why? Are there any additional disclosures relating to joint arrangements that would be useful for users of financial statements?

<u>The disclosure requirements need to be reassessed</u>

The IASB has not clearly articulated its rationale as to why the proposed disclosure is required. Accordingly, it is difficult to opine as to whether the information is useful to the users of the financial statements when the only available reference is to historical practice.

In essence, the need for so much disclosure in the proposed Standard is a reflection of the fact that the accounting methodology proposed is not necessarily an optimal solution. Ideally, the accounting methodology adopted should of itself convey much of the information that users require, with additional footnote disclosure being limited to that which is absolutely necessary and which users find useful.

Accordingly, we believe that the disclosure requirements of the proposed Standard could be streamlined and improved. In addition, the IASB needs to clearly articulate its rationale for including the disclosures required by the proposed Standard. The disclosures required should be informative and useful without being overly burdensome. It is incumbent upon the IASB to illustrate why the disclosures required are relevant and useful to the needs of the users of financial statements.

Therefore, we recommend that the disclosure section of the proposed Standard be recast, clearly setting out the core disclosure objectives and summaries of disclosures that meet those core objectives, in a similar way to the approach taken in Standards such as IFRS 2 *Share-based Payment* and IFRS 3 *Business Combinations*. We note that many of the existing proposals are more in the nature of guidance rather than an articulation of core objectives and principles.

<u>Detailed comments on the existing proposals in ED 9 in the event the IASB proceeds with this project</u>

As noted above, we recommend that the IASB recast the disclosure requirements, clearly setting out the core disclosure objectives and summaries of disclosures that meet those core objectives.

However, in the event that the IASB decides to proceed with the existing approach to disclosure, we suggest that the disclosure requirements be improved in the following manner:

- Paragraph 36 could form the basis of a key disclosure principle of the proposed Standard, but it should be reworded to better explain the core objective of the disclosures required – we would consider the first sentence of paragraph 39 could also form part of this objective;
- The nature of the entity's interests in all forms of joint arrangements should be a required disclosure; and
- The financial impact of joint arrangements on the financial statements should also be disclosed.

To the extent relevant, these disclosures could also be duplicated in IAS 27 and IAS 28.

Disclosure proposals that we do not support

In addition to our general comments above, we do not agree with the following disclosure requirements that are proposed in ED 9:

- The requirement to disclose information for each individually material joint venture. We believe that this is onerous and will provide little benefit to the users of financial statements, particularly for large corporate entities participating in the extractive and real estate industries where there may be many such ventures. We also note that the consequential amendments to IAS 28 are inconsistent with these proposals as the disclosures under a revised IAS 28 would not require information for each individually material investment over which an entity has significant influence. We would prefer that the proposed Standard mirror the requirements proposed for IAS 28; and
- The requirement to disclose the current and non-current amounts of joint ventures (as noted in our response to question 6 below).

Convergence with US GAAP has not been fully achieved

We note that the proposed disclosure requirements are not fully consistent with the equivalent US GAAP requirements in APB Opinion No. 18 *The Equity Method of Accounting for Investments in Common Stock* (APB 18). Specifically:

- The proposed requirements in paragraphs 37, 38, 39(c), 39(d), 39(e), 40 and 41 of ED 9 are not required under APB 18 – we recommend that these proposed disclosure requirements be reassessed on a cost-benefit basis for inclusion in any final Standard resulting from ED 9;
- APB 18 has the following additional disclosure requirements that are not present in ED 9 – in the event that a full joint convergence project with the FASB is not undertaken on joint arrangements, we recommend that, at a minimum, these additional disclosures be considered (as relevant) for inclusion in the final Standard resulting from ED 9:
  - paragraph 20(a), requiring information about the difference between the amount at which an investment is carried and the amount of underlying equity in net assets and the accounting treatment of the difference;
  - paragraph 20(b), requiring disclosure of the market value of an investment based on the quoted market price (where available); and

- paragraph 20(e), requiring disclosure of the material effects of possible conversions of convertible securities, exercises of outstanding options and warrants or other contingent issuances.

Question 5: Do you agree with the proposal to restore to IAS 27 and IAS 28 the requirements to disclose a list and description of significant subsidiaries and associates? If not, why?

We agree with this proposal.

Question 6: Do you agree that it is more useful to users if an entity discloses current and non-current assets and liabilities of associates than it is if the entity discloses total assets and liabilities? If not, why?

As noted in our responses to the questions above, the IASB has not clearly articulated its rationale as to why this disclosure is required. Accordingly, it is difficult to opine as to whether the information is useful to the users of the financial statements.

Appendix B – Drafting comments

The following are miscellaneous drafting comments that we recommend the IASB considers in finalising any IFRS resulting from ED 9:

Definitions and terminology

- We prefer the use of the term "jointly controlled ventures" rather than "joint ventures" so that these arrangements are more clearly distinguished from other joint arrangements within the scope of the proposed Standard.
- Paragraph 5 of the proposed Standard states that "an entity is a party to a joint venture if it has rights only to a share of the outcome generated by a group of assets and liabilities carrying on an economic activity". We recommend that this be amended to also refer to the situation where there is a single asset, such as an interest in an investment property, pipeline or similar arrangement. We suggest that this be amended to *"generated by an asset or group of assets and liabilities…"*
- In order to achieve consistency in wording, we recommend that paragraph 11 of the proposed Standard be amended to include a reference to "joint arrangement" in the same way as for the other types of joint arrangements (in paragraphs 8 and 15), i.e. *"A joint asset is a joint arrangement, or part of a joint arrangement, where each party has rights, and often has joint ownership, of an asset"*

Accounting requirements

- Paragraph 30 of the proposed Standard requires a retained interest to be measured at fair value on a loss of joint control. We recommend that an exemption for unquoted equity instruments whose fair value cannot be reliably measured be introduced into this requirement, equivalent to that available in IAS 39 *Financial Instruments: Recognition and Measurement* for these types of instruments.
- The last sentence of paragraph 32 deals with a reduction in ownership of a joint venture interest which remains a joint venture – this is not a 'loss of joint control' and should be moved to an appropriate place in the final IFRS.

Disclosures

- Paragraph 37(b) should be reworded to remove the reference to the word "incurred".
- The requirements of paragraph 41 are not a disclosure requirement and should be moved to an appropriate place in the proposed Standard.

Illustrative Examples

- Example 1 appears to deal with both a "joint operation" and a "joint venture". We recommend that consideration be given to amending the heading of the example to reflect this fact.
- Example 4 refers to "strategic decisions" rather than the wording used in the definition of "joint control". We recommend that the wording be amended to reflect the sharing of power to govern the operating and financial policies.
- Example 7 includes disclosure of the revenue expected to be generated by the arrangement. We question whether this disclosure is required by the proposed Standard and the usefulness and meaning of such disclosure.