

FINANCIAL SERVICES

International Financial Reporting Standards (IFRS) 10 Consolidated Financial Statements



Control

In May 2011 the IASB published IFRS 10 *Consolidated Financial Statements*. It supersedes IAS 27 *Consolidated and Separate Financial Statements* and SIC-12 *Consolidation - Special Purpose Entities*.

Non-Controlling Interest

ED 2011/4 Investment Entities

IFRS 11 Joint Arrangements

IFRS 12 Disclosure of Interest in Other Entities

Control

IFRS 10 defines the principle of control as the basis for determining which entities a parent entity should consolidate in the consolidated financial statements. It also confirms the existing principle that a parent entity should publish consolidated financial statements for entities controlled, using uniform accounting principles and fully eliminate intra-group items.

An investor should determine whether it is a parent by assessing whether it controls the investee. The requirements of IFRS 10 have changed the definition of control to situations when all of the following three elements of control are present:

- Power over the investee ;
- Exposure to, or rights to, variable returns from the entity's involvement with the investee; and
- The ability to affect the amount of returns through its powers over the investee.

The power over an investee arises from the existing right and/or contractual arrangement that gives the parent entity the current ability to direct the activities that significantly affects the return from an investee. It also needs to be determined that the practical ability to exercise control over the investee is not prevented by for example legal or regulatory reasons.

Variable returns may include dividends, interest from debt securities, change in the value of investment, remuneration for services performed for the investee, cost savings achieved through economies of scale, and other circumstances that would have an impact on return such as access to proprietary knowledge.

In straight forward cases the new definition of control will not change the scope of consolidation. Changes are more likely to affect the accounting for non-straightforward cases for example investments in Special Purpose Entities.

Non-Controlling Interest

If a parent has a non-controlling interest it shall present its interest in the consolidated statement of financial position within equity, separately from the equity of the owners of the parent.

The effective date for IFRS 10 is 1 January 2013 and will be applied retrospectively for the comparative year. Early adoption is permitted but IFRS 11 (see below), IFRS 12 (see below), IAS 27 and IAS 28 (as amended) must be applied at the same time.

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ED 2011/4 Investment Entities

Currently investment activities are subject to the same consolidation requirements as other entities. Under the proposal, set out in the ED 2011/4, an investment entity would not be required to consolidate those investments that it controls provided that:

- The entity meet certain criteria;
- That the entity accounts for the investments in subsidiaries, associates and joint ventures at fair value through profit and loss; and
- Extensive disclosures are provided about the investment activities are provided in the financial statements.

The ED 2011/4 is intended to apply to entity such as funds with many investors and will, if adopted, be integrated within IFRS 10. The parent of an investment entity does not itself qualify as an investment entity and will not be able to use the exemption from consolidation.

IFRS 11 Joint Arrangements

This standard was also issued by the IASB in [May 2011] and replaces IAS 31 *Interests in Joint Ventures and SIC -13 Jointly Controlled Entities*.

IFRS 11 should be applied to all joint arrangements being an arrangement in which two or more parties has joint control arising from a contractual agreement of sharing control of an arrangement. A key feature is that all decisions about relevant activities require the consent of all parties.

IFRS 11 divides joint arrangements into two types for which the accounting will differ:

- Joint operations – in which the parties that have joint control have rights to the assets and obligations to the liabilities of the joint arrangement. Each joint operator will account for its assets , liabilities, revenue and expenses resulting from its interest in the joint operation, under the contractual arrangement between the parties,
- Joint venture – in which the parties that have joint control have rights to the net assets of the joint arrangement. The parties of a joint venture should account for its interest using the equity method under IAS 28 *Investments in Associated and Joint Ventures*.

A party that participates in, but does not have joint control of, a joint venture shall account for its interest in the arrangements in accordance with IFRS 9 *Financial Instruments*, unless it has significant influence over the joint venture, in which case it shall account for it in accordance with IAS 28 (as amended in 2011). Proportionate consolidation has been removed and is no longer permitted under IFRS 11.

The effective date for IFRS 11 is 1 January 2013 with earlier adoption permitted.

IFRS 12 Disclosure of Interest in Other Entities

IFRS 12 *Disclosure of Interest in Other Entities* was published in May 2011. It sets out the enhanced disclosure requirements of interest in other entities in a combined standard requiring application by entities that have an interest in any of the following:

- Subsidiaries;
- Joint arrangements (joint operations or joint ventures, as described in the section above);
- Associates; or

Unconsolidated structured entities.

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IFRS 12 does not apply to post-employment or other long-term benefit plans, an entity's separate financial statements, interest held in a joint arrangement in which the entity does not have joint control, or some interests in other entities that are accounted for in accordance with IFRS 9 *Financial Instruments*.

The objective of IFRS 12 is to require an entity to disclose information that enables the users of the financial statements to evaluate:

- the nature of, and risks associated with, its interests in other entities; and
- the effects of those on the financial position, financial performance and cash flows.

IFRS 12 specifies the minimum disclosures that an entity must provide. Below is an overview of the main disclosures required (although not a complete summary of all disclosure requirements):

Significant judgement and assumptions

An entity shall disclose information about significant judgements and assumptions it has made (and changes to those) in determining:

- that it has control of an entity;
- that it has joint control of an arrangement or significant influence over another entity; and
- the type of joint arrangement (joint operation or joint venture) when the arrangement has been structured through a separate vehicle.

Interests in subsidiaries

An entity shall disclose information that enables users of its financial statements to:

- understand the composition of the group;
- understand the interest that non-controlling interests have in the group's activities and cash-flows;
- evaluate the nature and extent of significant restrictions on its ability to access or use assets, and settle liabilities, of the group;
- evaluate the nature of, and changes in, the risks associated with its interest in consolidated structured entities;
- evaluate the consequences of changes in its ownership interest in a subsidiary that do not result in loss of control; and
- evaluate the consequences of losing control of a subsidiary during the reporting period.

Interest in joint arrangements and associates

An entity shall disclose information that enables users of its financial statements to evaluate:

- the nature, extent and financial effects of its interest in joint arrangements and associates, including the nature and effects of its contractual relationship with other investors with joint control, or significant influence over joint arrangements and associates; and
- the nature of, and changes in, the risks associated with its interest in joint ventures and associates.

Interest in unconsolidated structured entities

An entity shall disclose information that enables users of its financial statements to:

- understand the nature and extent of its interest in unconsolidated structured entities; and
- evaluate the nature of, and changes in, the risks associated with its interest in unconsolidated structured entities.

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If the minimum disclosures required by the standard are not sufficient to meet the disclosure objective, a reporting entity must disclose any additional information that is necessary to meet that disclosure objective.

The effective date for IFRS 12 is 1 January 2013. Early adoption is permitted.

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