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LKAS 31
Interests in Joint Ventures

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A Presentation to Interests in Joint Ventures
25 June 2012

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Introduction

Applicable Accounting Standard and Standard Interpretations

- LKAS 31 – Financial Reporting of Interests in Joint Ventures
- SIC-13 – Jointly Controlled Entities – Non-Monetary Contributions by Venturers

Scope

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Scope of LKAS 31

Covers

- accounting for interests in Joint Ventures, and the
- reporting of Joint Venture assets, liabilities, income and expenses in the financial statements of venturers and investors

(This is regardless of the structure or form under which the joint venture activities take place.)

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Scope of LKAS 31 (Contd.)

Not covers

- Venturers' interests in jointly controlled entities held by:

  (a) venture capital organisations, or

  (b) mutual funds, unit trusts and similar entities including investment-linked insurance funds

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Definitions

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Definitions

Joint Venture – a contractual agreement whereby two or more parties undertake an economic activity that is subject to joint control.

Joint Control – the contractually agreed sharing of control over an economic activity.

Control – the power to govern the financial and operating policies of an economic entity so as to obtain benefits from it.

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The contractual agreement

- Distinguishes interests with Joint Control from those where the investor has a significant influence

- Ensures no single venturer is in a position to exert universal control

Within LKAS 31, activities with no contractual arrangement to establish joint control are not joint ventures

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Different Forms of Joint Ventures

Jointly Controlled Entities	Jointly Controlled Operations	Jointly Controlled Assets
An entity is created and jointly controlled	Each venturer bears own costs and takes a share of the proceeds	An asset that is shared and jointly controlled
Separate legal entity formed	No legal entity formed	

Accounting for the different forms of Joint Ventures

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Accounting topics

- Accounting for:
  - Jointly Controlled Operations
  - Jointly Controlled Assets
  - Jointly Controlled Entities
- When to start and finish recording a Joint Venture
- Formation of a Joint Venture

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Accounting for Jointly Controlled Operations

Balance Sheet:	*- The assets it controls* *- The liabilities it incurs.*
Income Statement:	*- The expenses it incurs* *- The share of expenses it incurs jointly* *- The share of income it earns from the sale of goods or services by the Joint Venture.*

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Accounting for Jointly Controlled Assets

Balance Sheet:	*- Share of jointly controlled assets* *- Share of jointly incurred liabilities* *-Own liabilities relevant to the Joint Venture*
Income Statement:	*- Income from sale or use of its share of the Joint Venture output* *- Share of any Joint Venture expenses* *- Own expenses relevant to the JV.*

Accounting for Jointly Controlled entities

<u>Benchmark treatment</u>
Proportionate Consolidation

<u>Alternative treatment</u>
Equity Method

Two methods

Combine assets, liabilities, income and expenses on a <u>line by line basis</u>.

Include <u>separate lines</u> for each of assets, liabilities, income and expenses

Exceptions to benchmark and alternative treatment

- **The proportionate and equity methods are inappropriate where:**
  - **- Interest in a jointly controlled entity acquired and held exclusively with a view to its subsequent disposal in the near future**
  - **- Entity operates under severe long-term restrictions**
- **The interest should in these cases be presented in accordance with SLRS 9, Financial Instruments**

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Formation of Joint Venture

- No guidance with LKAS
- Best Practice suggests
  - Step up method
  - Predecessor method

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Transactions between Venturer and Joint Venture

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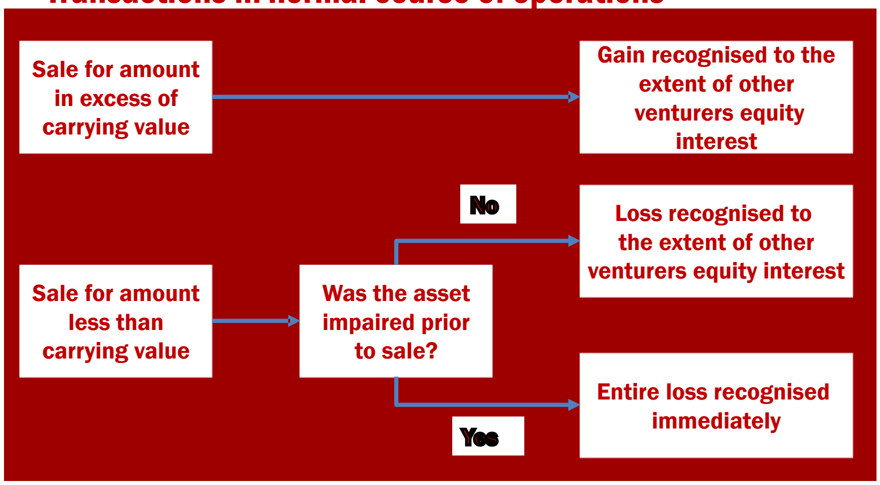
Transactions in normal course of operations



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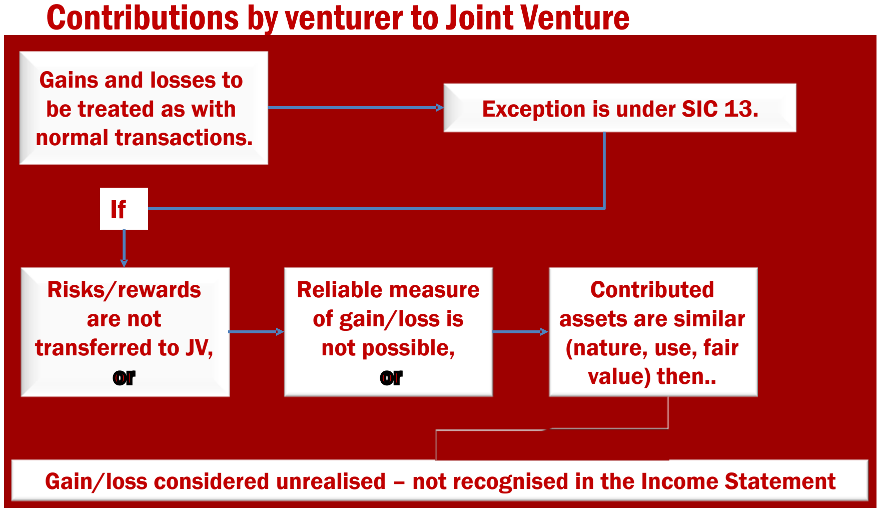
Contributions by venturer to Joint Venture



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Scenario

- C is a business venture that is jointly controlled by A and B
- Both use the proportionate consolidation method of accounting for their investment in C
- On 1 January 2011 A sells a warehouse for 150,000 in cash to C
- The warehouse has a book value of 80,000 and a useful life of 10 years after its transfer to C

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Question

What is the gain reported by A in its consolidated accounts as of 31 December 2011

A can only recognise income on this transaction to the value of the amount of profit attributable to the other venturer, B = 70,000 x 50% = 35,000.

Therefore only half of the apparent gain should be reported in A's accounts.

The unrealised portion of the gain should be eliminated against A's share of the asset now carried on the balance sheet of C. Thus (50% of 150,000 = 75,000) less the unrealised gain of (35,000) leaves a net of 40,000.

This 40,000 represents A's remaining interest (50%) in the asset – which is in fact equal to A's share of the original asset had the gain not been recorded.

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Question

When could the remainder of the gain be recognised?

When the asset is sold by the Joint Venture or as it is depreciated by the Joint Venture, the remaining profit of (70,000 x 50%) 35,000 can be recognised.

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Question

Would the treatment be different if the asset was inventory?

No – the only difference is that inventory is likely to be sold sooner and so the remainder of the gain is likely to be recognised sooner

Question

How will a venturer record a sale of the asset to the Joint Venture for an amount less than the carrying value in the accounts of the venturer?

The loss will be accounted for in exactly the same way as the gain as described above – that is, to the extent of the equity interests of the other venturers in the Joint Venture.

For example, if the warehouse was sold at a loss of 70,000, then A could recognise a loss of 35,000 at the time of the transaction.

If however, the loss provides evidence that the asset should have been written down in the accounts of the venturer prior to the sale (on Impairment or a Reduction in the Net Realisable Value of the asset) the entire loss on the sale of 70,000 should be recognised by the venturer in its income statement immediately.

Question

What does A report as its share of the warehouse held by C at 31 December 2011?

C will depreciate the asset at a rate of 10% per year, therefore at the end of 2011 the value would be 150,000 – 15,000 = 135,000

A's interest in this is 50% = 67,500

The unrealised gain of 35,000 is amortized in proportion to the depreciation charged by C. Therefore at the end of 2011 the value would be 35,000 –3,500 = 31,500

Thus the net reported amount of A's share is (67,500 – 31,500) = 36,000

This is in fact equal to A's share of the original asset less one years depreciation (40,000 – (40,000/10) = 36,000)

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Answer

In summary

Description	Calculation	Amount

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Disclosures

Disclosures

- Accounting policy
- Listing and description of interests including the proportion of ownership interest held in jointly controlled entities
- Aggregate amounts of Current Assets, Long Term Assets, Current Liabilities, Long Term Liabilities, Income and Expenses
- Commitments and contingencies
- Related party transaction disclosures per LKAS 24 – Joint Venture is a related party

Transitional provisions and effective date

An entity shall apply this Standard for annual periods beginning on or after 1 January 2012. Earlier application is encouraged. If an entity applies this Standard for a period beginning before 1 January 2012, it shall disclose that fact.

Thank you.