

STAFF PAPER

November 2014

IFRS Interpretations Committee Meeting

Project	IFRS 11 <i>Joint Arrangements</i>		
Paper topic	Proposed wording for Agenda Decision		
CONTACT(S)	Won-Hee Han	whan@ifrs.org	+44 (0)20 7246 6960

This paper has been prepared by the staff of the IFRS Foundation for discussion at a public meeting of the IFRS Interpretations Committee. Comments made in relation to the application of an IFRS do not purport to be acceptable or unacceptable application of that IFRS—only the IFRS Interpretations Committee or the IASB can make such a determination. Decisions made by the IFRS Interpretations Committee are reported in *IFRIC Update*. The approval of a final Interpretation by the Board is reported in *IASB Update*.

Introduction

1. At its meeting in September 2014, the IFRS Interpretations Committee (the Interpretations Committee) discussed how it can best document its conclusions and observations from the discussion of various issues relating to IFRS 11 that it had identified at its November 2013 meeting and had discussed at subsequent meetings up to July 2014.
2. The Interpretations Committee decided that the most appropriate way of documenting its work is to publish it in *IFRIC Update* rather than develop a new form of communication. In addition, the Interpretations Committee discussed the style of the documentation, and thought that a series of separate agenda decisions, each describing a separate aspect of its discussions, and capable of standing alone would be preferable. Consequently, the Interpretations Committee asked the staff to prepare separate summaries of each topic that has been discussed.
3. In response to the request of the Interpretations Committee, this paper proposes the wording (ie the summary of discussion) to be included in the section of ‘Interpretations Committee tentative agenda decisions’ of the November 2014 *IFRIC Update*. This paper also highlights some key points that can help the Interpretations Committee finalise the wording for (tentative) agenda decisions.

Proposed wording

Overview

4. As mentioned in the previous section of this paper, we propose issuing separate tentative agenda decisions for each topic as follows.
- (a) **(Agenda Decision A)** Classification of joint arrangements: the assessment of ‘other facts and circumstances’ (discussed at the Interpretations Committee meetings in November 2013, January 2014, March 2014 and May 2014);
 - (b) **(Agenda Decision B)** Classification of joint arrangements: application of ‘other facts and circumstances’ to specific fact patterns (discussed at the Interpretations Committee meetings in November 2013, January 2014 and March 2014);
 - (c) **(Agenda Decision C)** Classification of joint arrangements: consideration of an industry-specific case (discussed at the Interpretations Committee meetings in November 2013, January 2014, March 2014 and July 2014);
 - (d) **(Agenda Decision D)** Classification of joint arrangements: consideration of two joint arrangements with similar features that are classified differently (discussed at the Interpretations Committee meetings in November 2013, January 2014, March 2014 and July 2014);
 - (e) **(Agenda Decision E)** Accounting by the joint operator: recognition of revenue by a joint operator (discussed at the Interpretations Committee meetings in November 2013 and July 2014);
 - (f) **(Agenda Decision F)** Accounting by the joint operator: the accounting treatment when the joint operator’s share of output purchased differs from its share of ownership interest in the joint operation (discussed at the Interpretations Committee meetings in November 2013 and July 2014);
 - (g) **(Agenda Decision G)** Accounting in separate financial statements: accounting by the joint operator in its separate financial statements (discussed at the November 2013 Interpretations Committee meeting); and
 - (h) **(Agenda Decision H)** Accounting in separate financial statements: accounting by the joint operation in its financial statements (discussed at the

Interpretations Committee meetings in November 2013, January 2014¹, May 2014 and July 2014).

Consideration of key points for finalising the wording

5. In this section, we highlighted some key points that can help the Interpretations Committee finalise the wording. The key points include:
 - (a) terms in the proposed wordings that have been changed from those used in prior *IFRIC Updates*;
 - (b) conclusions of the Interpretations Committee that need confirmation; and
 - (c) major comments that have been received from the Interpretations Committee while drafting this paper and that have, or, have not, been reflected in this paper, and why they are, or are not, reflected.
6. We identified the key points for each (tentative) agenda decision as noted in paragraph 4 of this paper.

(Agenda Decision A) Point 1—deletion of the terms ‘direct’ and ‘in substance’

7. We had used the terms ‘direct rights and obligations’ and ‘in substance rights and obligations’ in prior *IFRIC Updates* and staff papers for the purpose of distinguishing between the rights and obligations of the parties to the joint arrangement, relating to the joint arrangement that are specified by the terms of the contractual arrangement (ie ‘direct’ rights and obligations) and the rights and obligations that are established through the assessment of ‘other facts and circumstances’ (ie ‘in substance’ rights and obligations).
8. Two Interpretations Committee members suggested deleting the terms ‘direct’ and ‘in substance’ because IFRS 11 does not use those terms. Accordingly, we have reflected this drafting suggestion.

¹ In the January 2014 meeting, the Interpretations Committee requested the staff to address issues relating to separate financial statements.

9. We therefore ask the Interpretations Committee whether it agrees with the deletion of the terms ‘direct’ and ‘in substance’.

(Agenda Decision A) Point 2—exclusion of the discussion involving the term ‘piercing the veil of incorporation’

10. We had used the term ‘piercing the veil of incorporation’ in prior staff papers when addressing the assessment of ‘other facts and circumstances’². However, we did not include the discussion involving the term ‘piercing the veil of incorporation’ because an Interpretations Committee member raised in the September 2014 Interpretations Committee meeting that using the term was confusing, and also another Interpretations Committee member said, while reviewing a draft of this paper, that the discussion involving the term ‘piercing the veil of incorporation’ is not relevant to the assessment of ‘other facts and circumstances’.
11. We therefore ask the Interpretations Committee whether it agrees with the exclusion of the discussion involving the term ‘piercing the veil of incorporation’.

(Agenda Decision A) Point 3—deletion or relocation of “implication of ‘economic substance’”

12. We have changed a subtitle from “implication of ‘substance over form’” to “implication of ‘economic substance’” reflecting a comment from an Interpretations Committee member.
13. Meanwhile, another Interpretations Committee member suggested deleting this section or relocating it to Agenda Decision D, which deals with a matter that relates to a circumstance in which two joint arrangements with similar features are classified differently depending on whether or not the joint arrangement is structured through a separate vehicle.
14. Accordingly, we ask the Interpretations Committee to agree on one of the alternatives:

² Although the term ‘piercing the veil of incorporation’ was used in the November 2013 *IFRIC Update*, it was not used in the context of the assessment of ‘other facts and circumstances’.

- (a) (Alternative A) keeping this section in the current location (ie Agenda Decision A);
- (b) (Alternative B) deleting this section; or
- (c) (Alternative C) relocating this section to Agenda Decision D.

(Agenda Decision B) Point 4—appropriateness of Agenda Decision B

- 15. One Interpretations Committee member commented that the specific fact patterns in Agenda Decision B were not documented in the IFRIC *Update* previously and it is therefore essential that the Interpretations Committee agree on how to publish Agenda Decision B.
- 16. We therefore ask the Interpretations Committee whether it agrees to publish Agenda Decision B.

(Agenda Decision B) Point 5—deleting the conclusion of the section “Determining the basis for ‘substantially all of the output’”

- 17. One Interpretations Committee member suggested deleting the conclusion of the subsection “Determining the basis for ‘substantially all of the output’” because the Interpretations Committee member thinks it would be interpretative. The conclusion is currently worded to read that “Consequently, it noted that the assessment is based on the monetary value of the output, rather than on physical quantities.”
- 18. We therefore ask the Interpretations Committee whether it agrees with deleting the conclusion of the subsection “Determining the basis for ‘substantially all of the output’” as suggested by one Interpretations Committee member.

(Agenda Decision C) Point 6—focusing on principles rather than on specific features

- 19. One Interpretations Committee member expressed a concern that Agenda Decision C concludes on an industry– and structure–specific fact patterns. This Interpretations Committee member suggested focusing on generic principles in the context of a party

being a primary obligor and saying that the Interpretations Committee would not address specific fact patterns.

20. We did not reflect this comment, but instead we have included an alternative wording for Agenda Decision C, which reflects this comment in **Appendix A** of this paper.
21. We therefore ask the Interpretations Committee to agree with the proposed wording for Agenda Decision C or an alternative wording as in Appendix A.

(Agenda Decision E) Point 7—how to describe the reason why paragraph 20(d) of IFRS 11 would not be applicable

22. Two Interpretations Committee members expressed different views on describing why paragraph 20(d) of IFRS 11 would not be applicable.
23. One Interpretations Committee member thinks that it is related to general consolidation procedures. In other words, the share of the revenue from the sale of the output to the joint operators by the joint operation would be eliminated against the share of the output purchased by the joint operators.
24. On the other hand, the other Interpretations Committee member thinks that applying a consolidation procedure is not appropriate as the reason why paragraph 20(d) of IFRS 11 would not be applicable. This Interpretations Committee member thinks that paragraph 20(d) of IFRS 11 does not apply because the sale of the output by the joint operation to the joint operator would mean selling output to itself and therefore, joint operator would not recognise the share of the revenue from the sale of the output by the joint operation.
25. We note that avoidance of the reference to ‘consolidation procedures’ helps to reinforce that joint operation accounting is not proportionate consolidation.
26. We therefore ask the Interpretations Committee to agree on one of the two views.

Staff recommendation

27. On the basis of the consideration of key points as noted above, we recommend that the Interpretations Committee reach an agreement on each point below.

Questions for Interpretations Committee

- 1 Does the Interpretations Committee agree with deleting the terms ‘in substance’ and ‘direct’ as noted for Point 1?
2. Does the Interpretations Committee agree with excluding the discussion involving the term ‘piercing the veil of incorporation’ from Agenda Decision A as noted for Point 2?
3. Does the Interpretations Committee agree with keeping the subsection ‘implication of economic substance’ in the current location (ie Agenda Decision A) as noted for Point 3?
4. Does the Interpretations Committee agree with publishing Agenda Decision B as noted for Point 4?
5. Does the Interpretations Committee agree with deleting the conclusion of the subsection “Determining the basis for ‘substantially all of the output’” in describing Agenda Decision B as noted for Point 5?
6. Does the Interpretations Committee agree with dealing with specific features for Agenda Decision C or focusing on principles (ie Alternative wording) as proposed in Appendix A as noted for Point 6?
7. Does the Interpretations Committee agree with describing the reason why paragraph 20(d) of IFRS 11 would not be applicable as currently drafted in Agenda Decision E as noted for Point 7?

Proposed wordings for tentative agenda decisions

28. The proposed wordings for each tentative agenda decision are as follows.
- (a) The proposed wording for Agenda Decision A is as follows:

IFRS 11 *Joint Arrangements*—Classification of joint arrangements: the assessment of ‘other facts and circumstances’

In May 2014, the Interpretations Committee published an agenda decision in the

IFRIC *Update* with regard to an issue of how an assessment of ‘other facts and circumstances’ as noted in paragraph 17 of IFRS 11 should be performed.

The Interpretations Committee considered whether the assessment of ‘other facts and circumstances’ should be undertaken with a view only towards whether those facts and circumstances create enforceable rights to the assets and obligations for the liabilities or whether that assessment should also consider the design and purpose of the joint arrangement, the entity’s business needs and the entity’s past practices.

The Interpretations Committee noted that paragraph 14 of IFRS 11 requires the classification of a joint arrangement as a joint operation or a joint venture to depend on rights to the assets and obligations for the liabilities of the parties to the arrangement, and that rights and obligations, by nature, are enforceable.

The Interpretations Committee also noted that paragraph B30 of IFRS 11 describes that when ‘other facts and circumstances’ give the parties rights to the assets, and obligations for the liabilities, relating to the arrangement, the assessment of ‘other facts and circumstances’ would lead to the joint arrangement being classified as a joint operation.

Consequently, the Interpretations Committee noted that the assessment of ‘other facts and circumstances’ should focus on whether those facts and circumstances create rights to the assets and obligations for the liabilities.

The Interpretations Committee also had further discussions about particular aspects of the assessment of ‘other facts and circumstances’. These are described below.

‘Implication of creating rights to the assets and obligations for the liabilities’

The Interpretations Committee discussed how and why particular facts and circumstances create rights and obligations that result in the joint arrangement being classified as a joint operation when the joint arrangement is structured through a separate vehicle.

The Interpretations Committee noted that the assessment of ‘other facts and circumstances’ is performed when there is no contractual arrangement to reverse or

modify the rights and obligations conferred by the legal form of the separate vehicle in which the arrangement has been structured. The assessment of ‘other facts and circumstances’ thus focuses on whether the ‘other facts and circumstances’ would establish for the parties to the joint arrangement rights to the assets and obligations for the liabilities, relating to the joint arrangement.

The Interpretations Committee, referring to paragraphs B31 and B32, observed that parties to the joint arrangement have rights to an asset of the joint arrangement through the assessment of ‘other facts and circumstances’ when they:

- have rights to substantially all of the economic benefits (for example, ‘output’) of an asset of the arrangement; and
- have obligations to acquire those economic benefits and thus assume the risks relating to those economic benefits (for example, the risks relating to the ‘output’).

The Interpretations Committee, referring to paragraphs B14, B32 and B33, also observed that parties to the joint arrangement have obligations for a liability of the joint arrangement through the assessment of ‘other facts and circumstances’ when they:

- settle a liability of the joint arrangement through providing cash flows as a consequence of the parties’ rights to and obligations for the assets; and
- settlement of the liability of the joint arrangement occurs in this manner on a continuous basis.

On the basis of its observations above, the Interpretations Committee noted that when the parties to a joint arrangement meet the criteria above and therefore have rights to an asset of the joint arrangement and obligations for a liability of the joint arrangement through the assessment of ‘other facts and circumstances’, a joint arrangement structured through a separate vehicle can be a joint operation.

Consequently, the Interpretations Committee observed that it is necessary to demonstrate that the parties to the joint arrangement have rights and obligations relating to economic benefits of the assets of the arrangement and provide cash through legal or contractual obligations to pay the liabilities of the joint

arrangement in order to classify the joint arrangement as a joint operation, as a result of assessing ‘other facts and circumstances’.

Implication of ‘economic substance’

Some members of the Interpretations Committee observed that the concept of ‘economic substance’ may not be consistently understood or applied in practice with regard to the assessment of ‘other facts and circumstances’.

The Interpretations Committee confirmed that the assessment of ‘other facts and circumstances’ should focus on whether the parties to the joint arrangement have rights to the assets, and obligations for the liabilities, relating to the joint arrangement. Consequently, the Interpretations Committee, by referring to paragraph BC43 of IFRS 11, noted that the consideration of ‘other facts and circumstances’ is not a test of whether the parties to the joint arrangement are closely or fully involved with the operation of the separate vehicle, but rather a test of whether ‘other facts and circumstances’ overcome the form of a separate vehicle.

On the basis of the analysis above, the Interpretations Committee determined that the assessment of ‘other facts and circumstances’ should be undertaken with a view towards whether those facts and circumstances create enforceable rights to an asset or obligations for a liability. That assessment is made in the light of the existing IFRS requirements. Accordingly, the Interpretations Committee concluded that sufficient guidance exists and that neither an Interpretation nor an amendment to a Standard was necessary. Consequently, the Interpretations Committee [decided] not to add this issue to its agenda.

- (b) The proposed wording for Agenda Decision B is as follows:

IFRS 11 *Joint Arrangements*—Classification of joint arrangements: application of ‘other facts and circumstances’ to specific fact patterns

The Interpretations Committee discussed how ‘other facts and circumstances’ should be applied to some specific fact patterns. It identified four different cases and considered how particular features of those fact patterns would affect the classification of the joint arrangement when assessing ‘other facts and circumstances’. The observations from the discussions are as follows.

Output sold at a market price

The Interpretations Committee discussed whether the fact that the output from the joint arrangement is sold to the parties of the joint arrangement at a market price prevents the joint arrangement from being classified as a joint operation, when assessing ‘other facts and circumstances’.

The Interpretations Committee observed that the sale of output from the joint arrangement to the parties at market price, on its own, is not a determinative factor for the classification of the joint arrangement. It noted that for example, the cash flow provided to the joint arrangement through the parties’ purchase of the output of the joint arrangement at market price might not be sufficient in some circumstances, in and of itself, to enable the joint arrangement to settle its liabilities on a continuous basis, depending on the market price.

Accordingly, the Interpretations Committee noted that exercising judgement based on other facts and circumstances that may give the parties’ rights to the assets and obligations for the liabilities, relating to the joint arrangement, is therefore needed to determine if the arrangement is a joint operation.

Financing from a third party

The Interpretations Committee discussed whether financing from a third party prevents a joint arrangement from being classified as a joint operation.

The Interpretations Committee noted that if the cash flows from the sale of output to the parties to the joint arrangement fund the repayment of the external financing, third-party financing, of itself, would not affect the classification of the joint arrangement.

Nature of output (ie fungible or bespoke output)

The Interpretations Committee discussed whether the nature of the output (ie fungible or bespoke output) produced by the joint arrangement determines the classification of a joint arrangement when assessing ‘other facts and circumstances’.

The Interpretations Committee noted that whether the output that is produced by the joint arrangement and purchased by the parties is fungible or bespoke is not a determinative factor for the classification of the joint arrangement. It noted that the guidance on the assessment of ‘other facts and circumstances’ in IFRS 11 does not consider the nature of output. It also noted that the focus of ‘obligation for the liabilities’ in IFRS 11 is on the cash flows between the parties and the joint operation, rather than the nature of the product (ie fungible or bespoke output).

Determining the basis for ‘substantially all of the output’

The Interpretations Committee discussed which of volumes of output or monetary values of output should be the basis for determining whether the parties to the joint arrangement are taking ‘substantially all of the output’ from the joint arrangement when assessing ‘other facts and circumstances’.

The Interpretations Committee, referring to paragraphs B31 and B32 of IFRS 11, noted that in order to meet the criteria for classifying the joint arrangement as a joint operation through the assessment of ‘other facts and circumstances:

- the parties to the joint arrangement should have rights to substantially all the ‘economic benefits’ of the assets of the joint arrangement; and
- the joint arrangement should be able to settle its liabilities from the ‘cash flows’ received as a consequence of the parties’ rights to and obligations for the assets of the joint arrangement.

The Interpretations Committee therefore noted that the ‘economic benefits’ of the assets of the joint arrangement would relate to the ‘cash flows’ arising from the

parties' rights and obligations for the assets. Consequently, it noted that the assessment is based on the monetary value of the output, rather than on physical quantities.

On the basis of the analysis above, the Interpretations Committee determined that, in the light of the existing IFRS requirements, sufficient guidance exists and that neither an Interpretation nor an amendment to a Standard was necessary.

Consequently, the Interpretations Committee [decided] not to add this issue to its agenda.

- (c) The proposed wording for Agenda Decision C is as follows (and an alternative wording for Agenda Decision C is in Appendix A):

IFRS 11 *Joint Arrangements*—Classification of joint arrangements: consideration of an industry-specific case

The Interpretations Committee discussed an issue relating to classification of a joint arrangement that was raised by several entities in the real estate industry. The concern was that a specific type of joint arrangement structure (so-called 'project entities') might be classified as a joint venture rather than a joint operation when applying IFRS 11; those entities who raised the concern thought that classifying 'project entities' as a joint venture would not reflect the economic substance of the joint arrangement.

The Interpretations Committee was presented with detailed features of 'project entities'; although 'project entities' have some common features, there were some variations to those features. Some key common features include:

- The joint arrangement is structured through a separate vehicle and is established for a bespoke construction project for delivery of a construction product or service to a (single) customer;
- The parties to the joint arrangement are heavily involved with the operation of the joint arrangement by, for example, providing a performance guarantee to customers for completion of the construction

and providing financing to the joint arrangement through cash calls (ie a commitment to provide cash on demand from the joint arrangement);

- The feature of the performance guarantee describes the parties to the joint arrangement as ‘primary obligors and not merely as sureties’, requiring them to effect specific performance resulting from non-performance of the joint arrangement; and it further describes that ‘even though the contract is signed between the joint arrangement and the customer, the position of parties to the joint arrangement are the same as if the contract had been signed directly by those parties’;
- In some cases, the construction in progress belongs to the (single) customer and therefore, in effect, the joint arrangement is the provision of construction and civil engineering *service* to the customer;
- The assets and liabilities of some joint arrangements are primarily cash, accounts receivable from customers, accounts payable to suppliers and non-financial liabilities in terms of the performance obligation.

The Interpretations Committee examined the detailed features and analysed: whether the parties to the joint arrangement have rights to the assets of the joint arrangement through the assessment of ‘other facts and circumstances’; and whether the parties to the joint arrangement have obligations for the liabilities of the joint arrangement through the assessment of ‘other facts and circumstances’.

The observations of the Interpretations Committee were as follows:

- The feature of the performance guarantee would be understood to put the parties to the joint arrangement in the same position as the joint arrangement (ie the separate vehicle) in terms of providing the product or service to the customer. For example, when the construction in progress belongs to a customer, the assets of the joint arrangement are primarily accounts receivables from the customer; these accounts receivables arise as a result of providing product or service to the customer; and therefore, the right to these accounts receivables may be shared by both the joint arrangement and the parties to the joint arrangement because the joint arrangement and the parties are in the same position with regard to the

obligation of providing product or service to the customer;

- On the basis of this observation, when considering the economic benefits of the assets in the joint arrangement, the parties to the joint arrangement would not have ‘substantially all’ the economic benefits of those assets even though they may have ‘some’ of the economic benefits. This is because the parties share the rights to the accounts receivables with the joint arrangement, which means the parties have ‘some of the rights to the accounts receivables, but not ‘substantially all’ of the rights to the accounts receivables.
- Accordingly, the parties to the joint arrangement would not have rights to the assets of the joint arrangement.
- On the other hand, the features could indicate that the parties to the joint arrangement have obligations for the liabilities of the joint arrangement, depending on the nature of the parties’ obligations. This is because, for example, the feature involving cash calls could indicate that the parties to the joint arrangement could be required to settle the liabilities of the joint arrangement on a continuous basis.

Consequently, the Interpretations Committee concluded that when taking into account the different features described above, the joint arrangement (ie ‘project entities’) would not be classified as a joint operation. This is because in order to classify a joint arrangement as a joint operation, the parties to the joint arrangement must have both rights to the assets, and obligations for the liabilities, relating to the joint arrangement, as noted in paragraphs B30–B32.

On the basis of the analysis above, the Interpretations Committee determined that, in the light of the existing IFRS requirements, sufficient guidance exists and that neither an Interpretation nor an amendment to a Standard was necessary.

Consequently, the Interpretations Committee [decided] not to add this issue to its agenda.

- (d) The proposed wording for Agenda decision D is as follows:

IFRS 11 *Joint Arrangements*—Classification of joint arrangements: consideration of two joint arrangements with similar features that are classified differently

The Interpretations Committee discussed a circumstance in which two joint arrangements with similar features are classified differently depending on whether or not the joint arrangement is structured through a separate vehicle (in circumstances in which the legal form confers separation between the parties and the separate vehicle). Such two joint arrangements could be classified differently:

- In the case of a joint arrangement that is structured through a separate vehicle, the legal form of the vehicle must be overcome by other contractual arrangements or specific ‘other facts and circumstances’ in order for the joint arrangement to be classified as a joint operation; but
- In the case of a joint arrangement that is not structured through a separate vehicle, classification as a joint operation is the default.

The Interpretations Committee noted that IFRS 11 could lead to two joint arrangements with similar features being classified differently if the principal difference between them is that one is structured through a separate vehicle and the other is not. This is because the legal form of the separate vehicle affects the rights and obligations of the parties to the joint arrangement when assessing the type of joint arrangement, as noted for example in paragraphs B22 and BC43 of IFRS 11.

The Interpretations Committee thought that such different accounting would not conflict with the concept of ‘economic substance’. This is because according to the approach adopted in IFRS 11, the economic substance means that the classification of the joint arrangement should reflect the rights and obligations of the parties to the joint arrangement and the presence of a separate vehicle plays a significant role in determining the nature of those rights and obligations.

The Interpretations Committee noted that the requirements of IFRS 11 provide the principles necessary for determining the classification of joint arrangements,

including assessing the impact of a separate vehicle. The assessment of the classification would depend on specific contractual terms and conditions and requires a full analysis of features involving the joint arrangement.

On the basis of the analysis above, the Interpretations Committee determined that, in the light of the existing IFRS requirements, sufficient guidance exists and that neither an Interpretation nor an amendment to a Standard was necessary.

Consequently, the Interpretations Committee [decided] not to add this issue to its agenda.

- (e) The proposed wording for Agenda Decision E is as follows:

**IFRS 11 *Joint Arrangements*—Accounting by the joint operator:
recognition of revenue by a joint operator**

The Interpretations Committee discussed whether a joint operator should recognise revenue in relation to the output purchased by the parties from the joint operation. This issue relates to the application of paragraph 20(d) of IFRS 11, which requires that a joint operator should recognise its share of the revenue from the sale of the output by the joint operation.

Examining paragraph 20(d) of IFRS 11, the Interpretations Committee noted that if the joint arrangement is structured through a separate vehicle and the assessment of ‘other facts and circumstances’ results in the joint arrangement being classified as a joint operation because the parties take all the output of the joint arrangement, paragraph 20(d) of IFRS 11 would not be applicable. This is because if the joint operators purchase all the output from the joint operation, they would recognise ‘their revenue’ when they sell the output to third parties.

In other words, the joint operators would not recognise any amount in relation to the ‘share of the revenue from the sale of the output by the joint operation’. This is because a joint operator with an obligation to purchase the output from the joint operation would result in that party having rights to the assets of the joint operation; accordingly, the sale of the output by the joint operation to the joint

operator would mean selling output to itself; and therefore, the joint operator would not recognise the share of the revenue from the sale of the output by the joint operation.

Accordingly, paragraph 20(d) of IFRS 11 would generally be applied to a joint operation when:

- the joint arrangement is not structured through a separate vehicle;
- the joint arrangement is structured through a separate vehicle and the contractual arrangement reverses or modifies the rights and obligations that are conferred by the legal form of the separate vehicle.

For example, a joint operator would recognise its share of the revenue from the sale of the output by the joint operation when the joint operation sells its output to third parties.

On the basis of the analysis above, the Interpretations Committee determined that, in the light of the existing IFRS requirements, sufficient guidance exists and that neither an Interpretation nor an amendment to a Standard was necessary.

Consequently, the Interpretations Committee [decided] not to add this issue to its agenda.

- (f) The proposed wording for Agenda Decision F is as follows:

IFRS 11 *Joint Arrangements*—Accounting by the joint operator: the accounting treatment when the joint operator’s share of output purchased differs from its share of ownership interest in the joint operation

The Interpretations Committee discussed the accounting when the joint operator’s share of the output purchased differs from its share of ownership interest in the joint operation.

For purposes of this discussion, the Interpretations Committee considered a fact pattern where the joint arrangement is structured through a separate vehicle and for

which the parties to the joint arrangement have committed to purchase substantially all of the output produced at a price designed to achieve a break-even result. In this fact pattern, the parties to the joint arrangement would be considered to have rights to the assets, and obligations for the liabilities. Such a joint arrangement is presented in Example 5 of the application guidance to IFRS 11 and is classified as a joint operation. A variation of such a fact pattern could (and does) arise in which the parties' percentage ownership interest in the separate vehicle differs from the percentage share of the output produced that each party is obliged to purchase.

The Interpretations Committee, referring to paragraph 20 of IFRS 11, noted that the joint operators of such a joint operation would account for their assets, liabilities, revenues and expenses in accordance with the shares specified in the contractual arrangement. However, when an assessment of 'other facts and circumstances' has been needed to conclude that the joint arrangement is a joint operation, and the joint arrangement agreement does not specify the allocation of assets, liabilities, revenues or expenses, the question arises about what share of assets, liabilities, revenue and expenses each joint operator should recognise. Specifically, should the share of assets, liabilities, revenue and expenses recognised reflect the percentage ownership of the legal entity, or should it reflect the percentage of output purchased by each joint operator?

The Interpretations Committee noted that there could be many different scenarios in which the joint operator's share of the output purchased differs from its share of ownership interest in the joint operation: for example, when the share of output purchased by each party varies frequently over the life of the joint arrangement, a question arising in this situation is over what time horizon should the share of output be considered.

The Interpretations Committee also noted that if the joint operators made a substantial investment in the joint operation that differs from their ownership interest, there may be an equalisation mechanism that could explain why there is a disconnection between the percentage ownership interest and the percentage share of the output produced that each party is obliged to purchase. It noted that such an equalisation mechanism may provide relevant information to determine how to

account for the difference between the two.

Consequently, the Interpretations Committee noted that it is important to understand why the share of the output purchased differs from the ownership interests in the joint operation. Judgement will therefore be needed to determine the appropriate accounting.

On the basis of the analysis above, the Interpretations Committee determined that, in the light of the existing IFRS requirements, sufficient guidance exists and that neither an Interpretation nor an amendment to a Standard was necessary. Consequently, the Interpretations Committee [decided] not to add this issue to its agenda.

- (g) The proposed wording for Agenda Decision G is as follows:

IFRS 11 *Joint Arrangements*—Accounting in separate financial statements: accounting by the joint operator in its separate financial statements

The Interpretations Committee discussed the issue of the accounting by a joint operator in its separate financial statements for its share of assets and liabilities of a joint operation when that joint operation is structured through a separate vehicle. The Interpretations Committee noted that IFRS 11 requires the joint operator to account for its rights and obligations in relation to the joint operation. It also noted that those rights and obligations are the same whether separate or consolidated financial statements are prepared, by referring to paragraph 26 of IFRS 11. Consequently the same accounting is required in the consolidated financial statements and in the separate financial statements of the joint operator.

The Interpretations Committee also noted that IFRS 11 requires the joint operator to account for its rights and obligations, which are its share of the assets held by the entity and its share of the liabilities incurred by it. Accordingly, the Interpretations Committee observed that the joint operator would not additionally account in its separate or consolidated financial statements for its shareholding in the separate vehicle, whether at cost in accordance with IAS 27 *Separate Financial*

Statements or at fair value in accordance with IFRS 9 *Financial Instruments*.

On the basis of the analysis above, the Interpretations Committee determined that, in the light of the existing IFRS requirements, sufficient guidance exists and that neither an Interpretation nor an amendment to a Standard was necessary.

Consequently, the Interpretations Committee [decided] not to add this issue to its agenda.

- (h) The proposed wording for Agenda Decision H is as follows:

IFRS 11 *Joint Arrangements*—Accounting in separate financial statements: accounting by the joint operation that is a separate vehicle in its financial statements

The Interpretations Committee discussed the issue of the accounting by the joint operation that is a separate vehicle in its financial statements. The recognition by joint operators in both consolidated and separate financial statements of their share of assets and liabilities held by the joint operation leads to the question of whether those same assets and liabilities should also be recognised in the financial statements of the joint operation itself.

The Interpretations Committee noted that IFRS 11 applies only to the accounting by the joint operators and not to the accounting by the separate vehicle that is a joint operation. The financial statements of the separate vehicle would therefore be prepared in accordance with applicable IFRS standards.

Company law often requires a legal entity/separate vehicle to prepare financial statements; therefore, the reporting entity for the financial statements would include the assets, liabilities, revenues and expenses of that legal entity/separate vehicle.

However, when identifying the assets and liabilities of the separate vehicle it is necessary to understand the joint operators' rights and obligations relating to those assets and liabilities and how those rights and obligations affect those assets and liabilities. The Interpretations Committee noted that it will be important to reflect

the effects of the joint operators' rights and obligations in the accounting for the joint operation's assets and liabilities. For example, the Interpretations Committee considered the two following examples:

- (a) In a circumstance in which a joint arrangement is structured through a separate vehicle, which sells the output to the parties to the joint arrangement, and therefore is classified as a joint operation,
 - (i) IFRS 11 requires the joint operators to account for the arrangement by recognising a share of the assets;
 - (ii) whereas the commitment of the joint operation to selling output would be an executory contract and therefore the separate vehicle would not account for the commitment unless it is onerous;
- (b) In a circumstance in which a joint arrangement is structured through a separate vehicle; and as part of the contractual agreement between the joint operator and joint operation there is a lease agreement whereby the joint operators have substantially all of the benefits of the leased assets, the separate vehicle would account for the leased asset in accordance with other Standards including IAS 17 *Leases*, while the joint operator would recognise its share of a leased asset as its own asset in accordance with IFRS 11. Accordingly, the lease agreement could cause the assets and liabilities of the joint operation to be derecognised in its own financial statements if the lease agreement qualifies as a finance lease.

On the basis of the analysis above, the Interpretations Committee determined that, in the light of the existing IFRS requirements, sufficient guidance exists and that neither an Interpretation nor an amendment to a Standard was necessary. Consequently, the Interpretations Committee [decided] not to add this issue to its agenda.

Staff recommendation

29. As proposed in the previous section, we recommend that the Interpretations Committee publish the tentative agenda decisions in the November 2014 IFRIC *Update*.

Questions for Interpretations Committee

8. Does the Interpretations Committee agree with the staff recommendation that the November 2014 IFRIC *Update* include agenda decisions for the issues as suggested in the proposed wording?
9. Does the Interpretations have any further suggestions on the proposed wording?

Appendix A—Alternative wording for Agenda Decision C**IFRS 11 *Joint Arrangements*—Classification of joint arrangements: parties are primary obligors**

The Interpretations Committee discussed an issue relating to classification of a joint arrangement in which the parties to the joint arrangement are primary obligors to the customer of the joint arrangement for the goods/services being provided. The issue considered was whether the obligations taken on by the parties were sufficient to lead to classification as a joint operation.

The key features of the joint arrangement were:

- The joint arrangement is structured through a separate vehicle.
- The parties to the joint arrangement are heavily involved in operation of the joint arrangement and the construction/delivery of the goods/services. The goods/services are sold to a third party customer.
- The parties provide financing to the joint arrangement through cash calls (ie a commitment to provide cash on demand from the joint arrangement).
- The customer owns the work in progress. The assets and liabilities of the joint arrangement are therefore primarily cash, accounts receivable from the customer, accounts payable to suppliers and non-financial liabilities in terms of a performance obligation.
- The parties to the joint arrangement provide a performance guarantee to the customer in which they are described as ‘primary obligors and not merely as sureties’, requiring them to effect specific performance resulting from non-performance of the joint arrangement. The performance guarantee describes the parties as being in the same position as if the contract with the customer had been signed by the parties themselves.

The Interpretations Committee observed, among other things, that the joint arrangement (that is the separate vehicle) is still a primary obligor regardless of the description in the performance guarantee of the parties as ‘primary obligors and not merely as sureties’.

Furthermore, the Interpretations Committee observed that the assets of the joint arrangement, being primarily accounts receivable from the customer, are assets to which the

rights may be shared by both the joint arrangement and the parties to the joint arrangement because the joint arrangement and the parties are in the same position with regard to providing the product or service to the customer.

Consequently, when considering the economic benefits of the assets in the joint arrangement, the parties to the joint arrangement would not have ‘substantially all’ the economic benefits of those assets even though they may have ‘some’ of the economic benefits. This is because the parties share the rights to the accounts receivable with the joint arrangement, which means that the parties have ‘some of the rights to the accounts receivable’ but not ‘substantially all’ of the rights to the accounts receivable.

The Interpretations Committee therefore concluded that the joint arrangement would not be classified as a joint operation because the parties have only some of the rights to the economic benefits of the assets of the joint arrangement rather than substantially all of the rights to the economic benefits of those assets.

On the basis of the analysis above, the Interpretations Committee determined that, in the light of the existing IFRS requirements, sufficient guidance exists and that neither an Interpretation nor an amendment to a Standard was necessary. Consequently, the Interpretations Committee [decided] not to add this issue to its agenda.