

December 2009

IASB Meeting December 2009

Agenda paper 10



Consolidation

The views expressed in this presentation are those of the presenters,
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The control model

2

'Power so as to benefit' model—power and the ability to use that power to generate returns for your own benefit

Power

- the current ability to enforce your will in directing the activities of an entity that significantly affect the returns (in the words of Statement No.167, the activities that most significantly impact that entity's economic performance)
- need not be absolute—others can have protective rights

Returns (benefits/losses)

- Vary with the activities of the entity
- Can be wholly positive, wholly negative or either positive or negative
- Others can share in the benefits/returns



The control model

3

Main decisions to date by both boards

- Control is the basis of consolidation
- Exposure to risks and rewards is an indicator of control
- Substantive participating rights (if sufficient) give a party power—could be voting rights, rights within other contractual arrangements, or a combination of these
- When multiple parties have unilateral decision-making authority over different activities, the party that has the ability to direct the activities that *most* significantly affect the returns meets the power element of the control definition
- When multiple parties share decision-making about the activities of the entity (and each party must consent to those decisions), no one party controls the entity [this is joint control in IFRS]



Consolidation

4

Upcoming joint Board discussions on:

- Control with less than half of the voting rights
- Assessment of control with options and convertible instruments
- Agent-principal analysis
 - Kick-out / removal rights
 - Remuneration of an agent
- Investment companies
- Disclosures for consolidated and unconsolidated entities



Less than half of the voting rights

5

Current IFRS and US GAAP:

- Consolidation with more than 50% of the voting rights
- Generally no consolidation with less than 50% (without rights in other contractual arrangements)

ED10 and 1999 FASB ED proposals:

- Entity can control with less than 50% (and without rights in other contractual arrangements)
- Feedback: operationality issues

Current staff thinking:

- Evidence of power required with less than 50% without rights in other contractual arrangements



Options and convertible instruments

6

Current IFRS and US GAAP:

- IFRS: currently exercisable options give the holder power
- US GAAP: not considered when assessing control

ED10 and 1999 FASB ED proposals:

- ED10: options can give the holder power (examples listed)
- 1999 FASB ED: options can give the holder power

Current staff thinking:

- Some think options do not give the holder power until exercised
- Some think options can give the holder power before exercise (additional factors to consider including currently exercisable and ability to benefit from exercise)



Kick-out (removal) rights

7

Current IFRS and US GAAP:

- IFRS: no specific guidance regarding kick-out rights
- US GAAP: guidance regarding substantive kick-out rights

ED10 and Statement No.167:

- ED10: removal (kick-out) rights considered as an indicator of an agency relationship
- Statement No.167: substantive kick-out rights exercisable by one party considered when assessing control

Current staff thinking:

- Some think kick-out rights must be exercisable by only one party to be substantive
- Some think there could be circumstances for which kick-out rights indicate an agency relationship (to be consider together with remuneration)



Remuneration of an agent

8

Current IFRS and US GAAP:

- No specific guidance regarding the remuneration of an agent.

ED10 and Statement No.167:

- ED10: nature of remuneration considered as an indicator of an agency relationship
- Statement No.167: any remuneration that is potentially significant meets the benefits element of the control definition

Current staff thinking:

- Remuneration is an indicator of an agency relationship. Additional guidance required regarding remuneration (to address dual role situations and performance-related fees).



Investment companies

9

Current IFRS and US GAAP:

- IFRS: controlled investments consolidated by investment companies
- US GAAP: controlled investments at fair value for investment companies

ED10:

- ED10: no change to current requirements
- Feedback from users: fair value provides the best information
- Input from the industry: proposals to define an investment company

Current staff thinking:

- On the basis of input from users, consider fair value reporting for investments controlled by investment companies (list of strict criteria defining an investment company)
- Also, a view may exist that investment companies should be subject to the consolidation guidance – no exception

