

STAFF PAPER

May 2014

IFRS Interpretations Committee Meeting

Project	IFRS 11 <i>Joint Arrangements</i>		
Paper topic	Feedback from consultations with IASB members		
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Introduction

1. As mentioned in Agenda Paper 2, at its March 2014 meeting, the IFRS Interpretations Committee (the Interpretations Committee) requested the staff to consult the IASB on how to apply the concept of ‘substance over form’ in assessing ‘other facts and circumstances’ in IFRS 11 *Joint Arrangements*.
2. In response to this request, the staff held a number of meetings with IASB members in April 2014 to obtain individual views from IASB members. This Agenda paper summarises the feedback from those consultations.

Information provided, and questions asked, to the IASB members

3. We provided IASB members with two views, View A (a narrow view) and View B (a broader view) on the notion of the application of ‘substance over form’ for assessing ‘other facts and circumstances’ when classifying a joint arrangement. The following is a summary of description of View A and View B provided to IASB members and questions asked to them.

View A (a narrow view)

4. The assessment of ‘other facts and circumstances’ focuses on whether the parties have ‘indirect’ rights and ‘indirect’ obligations¹, relating to the joint arrangement, that can be identified to be, in substance, ‘direct’ rights to the assets and ‘direct’ obligations for the liabilities, relating to the joint arrangement. So, if the entity has such ‘indirect’ rights and obligations, the joint arrangement would be classified as a joint operation.
5. View A can be described in a way that it is necessary to demonstrate that cash cascades from the parties to the joint arrangement, through legal or contractual obligations, to ensure the settlement of the liabilities of the joint arrangement on a continuous basis (ie cascading contractual rights and obligations).
6. Cascading contractual rights and obligations would ‘pierce the veil of incorporation’, which means that the boundaries of a separate vehicle are overcome, resulting in the parties having access to the assets of the separate vehicle and exposure to the liabilities of the separate vehicle.
7. View A is also based on the fact that IFRS 11 provides only one example² where assessing other facts and circumstances results in the joint arrangement being classified as a joint operation, that is, when the joint arrangement sells output to the parties to the joint arrangement. This suggests that the sale of output to the parties to the joint arrangement is critical to the classification decision.

¹ We used the term ‘inferred’ rights and ‘inferred’ obligations instead of ‘indirect’ rights and ‘indirect’ obligations in the Agenda papers (AP 5A and AP5B) presented at the March 2014 Interpretations Committee meeting for want of a better description.

² In addition to the example in the Application Guidance described, the Illustrative Examples to IFRS 11 include two examples of joint arrangements that are classified as joint operations in which there is an entity whose legal form confers separation between the parties and the entity. In both of those examples the parties to the joint arrangement are committed to purchasing the output of the joint arrangement. One of the examples includes a variation to the fact pattern in which the product is sold to third parties rather than the parties sharing joint control; the variation results in a change in classification from joint operation to joint venture.

View B (a broader view)

8. View B is broader than View A in terms of considering what can give rise to ‘indirect’ rights and ‘indirect’ obligations. Design, economic compulsion and business needs should also be taken into account.
9. In addition, if the parties to the joint arrangement are closely or fully involved with the operation of the separate vehicle, the classification as a joint operation would reflect the economic substance of the arrangement.

Questions asked to the IASB members

10. We consulted IASB members on whether the current requirements of IFRS 11 should be read to support a narrow interpretation of the role of ‘other facts and circumstances’ such as View A or a broader view, such as View B.
11. We also consulted IASB members on whether they agree with a view, as indicated by View A, that the joint arrangement would be classified as a joint venture if the separate vehicle sells substantially all of its output to third parties rather than the parties to the joint arrangement.

Feedback from consultations with IASB members

12. Almost all IASB members thought that View A is consistent with the current requirements of IFRS 11.
13. One IASB member thought that it was important for the Interpretations Committee to complete its work looking at certain joint arrangement structures (namely, the project entity structure), before a conclusion should be made about whether View B is inappropriate.
14. Meanwhile, some IASB members commented about the convergence with US GAAP. They noted that the joint arrangements project was an IASB project that was intended to reduce differences between IFRSs and US GAAP, although the requirements of IFRS 11 were not deliberated by the FASB. Those IASB members said that it would be useful to examine how different IFRS 11 would be from US GAAP in terms of the classification of the joint arrangement.

15. On the basis of the feedback from consultations with IASB members and discussions at previous Interpretations Committee meetings, we continue to think that the current requirements in IFRS 11 are consistent with View A.
16. We also think that the feedback is consistent with the tentative agenda decision on Issue 1A (ie should the assessment of ‘other facts and circumstances’ be based only on contractual (and legal) enforceable terms?³) at the January 2014 Interpretations Committee meeting.
17. Consequently, we think that the Interpretations Committee’s discussions on how consideration of ‘other facts and circumstances’ affect the classification of a joint arrangement do not need to be reassessed. We think that the Interpretations Committee can consider the next steps in its work on this topic and Agenda Paper 2C presents some alternative next steps, and a staff recommendation.

Questions for the Interpretations Committee

1. In the light of this feedback, does the Interpretations Committee have any questions or comments on the feedback from our consultations with IASB members?

³ At its January 2014 meeting, the Interpretations Committee agreed with a tentative agenda decision on this issue.