

Classification of joint arrangements: the assessment of ‘other facts and circumstances’ (IFRS 11 *Joint Arrangements*)—March 2015

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 each party’s rights to the assets and obligations for the liabilities of the joint arrangement, and that the rights and obligations are enforceable.

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

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

The Interpretations Committee also discussed how and why particular facts and circumstances create rights to the assets and obligations for the liabilities. This discussion is described in the following paragraphs.

How and why particular facts and circumstances create rights and obligations

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 whose legal form causes the separate vehicle to be considered in its own right.

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 through which the arrangement has been structured. The assessment of other facts and circumstances thus focuses on whether the other facts and circumstances establish, for each party 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–B32 of IFRS 11, observed that parties to the joint arrangement have rights to the assets of the joint arrangement through other facts and circumstances when they:

- a. have rights to substantially all of the economic benefits (for example, ‘output’) of assets of the arrangement; and
- b. 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 and B32–B33 of IFRS 11, also observed that parties to the joint arrangement have obligations for liabilities of the joint arrangement through other facts and circumstances when:

- a. as a consequence of their rights to, and obligations for, the assets of the joint arrangement, they provide cash flows that are used to settle liabilities of the joint arrangement; and
- b. settlement of the liabilities of the joint arrangement occurs on a continuous basis.

On the basis of these observations, the Interpretations Committee noted that when each party to a joint arrangement meets the criteria and therefore has both rights to the assets of the joint arrangement and obligations for the liabilities of the joint arrangement through other facts and circumstances, a joint arrangement structured through a separate vehicle is a joint operation.

Consequently, the Interpretations Committee observed that, in order to classify the joint arrangement as a joint operation as a result of assessing other facts and circumstances, it is necessary to demonstrate that:

- a. each party to the joint arrangement has rights and obligations relating to economic benefits of the assets of the arrangement; and
- b. each party is obliged to provide cash to the arrangement through enforceable obligations, which is used to settle the liabilities of the joint arrangement on a continuous basis.

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 each party to the joint arrangement has 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 each party to the joint arrangement is closely or fully involved with the operation of the separate vehicle, but is instead a test of whether other facts and circumstances override the rights and obligations conferred upon the party by the legal form of the separate vehicle.

On the basis of this analysis, 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 assets and obligations for liabilities. 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.