

PROPOSED FINANCIAL REPORTING STANDARD

ED/FRS 10

EXPOSURE DRAFT

CONSOLIDATED FINANCIAL STATEMENTS

Comments to be received by 6 February 2009

ED 10 *Consolidated Financial Statements* is issued by the Accounting Standards Council (ASC) for comment only and does not necessarily represent the views of ASC. The proposals may be modified in the light of the comments received before being issued as a Financial Reporting Standard (FRS).

Comments are most helpful if they indicate the specific paragraph or group of paragraphs to which they relate, clearly explain the problem and provide a suggestion for alternative wording with supporting reasoning.

Comments should be submitted in writing, so as to be received by 6 February 2009 preferably by email to MOF_Feedback_ASC@mof.gov.sg or addressed to:

Accounting Standards Council
c/o Ministry of Finance
100 High Street #10-01
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Introduction and invitation to comment

Introduction

- 1 It initiated its project on consolidated financial statements with the objective of publishing a single FRS on consolidation to replace the consolidation requirements in FRS 27 *Consolidated and Separate Financial Statements* and INT FRS 12 *Consolidation—Special Purpose Entities*. The main objectives of the project are to improve the definition of control and related application guidance so that a control model can be applied to all entities, and to improve the disclosure requirements about consolidated and unconsolidated entities.
- 2 [Not used]
- 3 The exposure draft proposes a single definition of control for all entities, and provides guidance on how to apply that definition in particular situations that have been found difficult when applying FRS 27 and INT FRS 12. As a consequence, it expects that entities will be consolidated on a more consistent basis, making the financial statements of groups more comparable and understandable.
- 4 In addition to the proposals in this exposure draft, it is also reviewing, in a separate project, its requirements for the derecognition of financial instruments. The derecognition of financial instruments sometimes involves the use of structured entities. Therefore the projects on consolidation and derecognition of financial instruments are closely related in those circumstances. It would have preferred to publish exposure drafts for these projects at the same time. However, in response to the wide demand for a revised consolidation standard, it decided not to delay publication of the consolidation exposure draft. It expects that it will be able to publish an exposure draft on the derecognition of financial instruments at the end of the first quarter or start of the second quarter of 2009.

Summary of the proposals and invitation to comment

- 5 The ASC seeks comment on whether the control definition proposed in this exposure draft, and the accompanying guidance on how to apply that definition, provides clearer guidance for determining when one entity controls another. It is also seeking comment on whether the enhanced disclosure requirements for consolidated and unconsolidated entities will give capital providers and other users of financial statements information that is useful for their decision-making.
- 6 The ASC invites comments on all matters in this exposure draft, and in particular on the questions set out in the following paragraphs. Respondents need not comment on all of the questions. Comments are most helpful if they:
 - respond to the questions as stated
 - indicate the specific paragraph or paragraphs to which the comments relate
 - contain a clear rationale
 - describe any alternatives it should consider.
- 7 It will consider all comments that it receives in writing by 6 February 2009.

Control

- 8 FRS 27 defines control as the power to govern the financial and operating policies of an entity so as to obtain benefits from its activities. Further guidance on when an entity should consolidate special purpose entities is provided in INT FRS 12. However, many have noted that the consolidation models in FRS 27 and INT FRS 12 differ. Some have indicated that

there can be difficulties determining whether particular entities are within the scope of FRS 27 or INT FRS 12, resulting in diversity in practice and reduced comparability of consolidated financial statements. Some are also concerned about the structuring incentives that those inconsistencies might have created.

9 This exposure draft proposes to address those inconsistencies by replacing the definition of control in FRS 27 and the indicators of control in INT FRS 12 with a single definition of control that would apply to all entities.

10 It proposes the following definition of control of an entity:

A reporting entity controls another entity when the reporting entity has the power to direct the activities of that other entity to generate returns for the reporting entity

11 Consequences of the definition are that only one party can control an entity and there could be circumstances in which an entity is not controlled by any party.

Power to direct the activities

12 Control of another entity requires the power to direct the activities of that other entity. It believes that the power to govern the financial and operating policies, as stated in FRS 27, is one means of having power to direct the activities of another entity, but it is not the only means. Power can be achieved in many ways, including by having voting rights, by having options or convertible instruments, by means of contractual arrangements, or a combination of these, or by having an agent with the ability to direct the activities for the benefit of the controlling entity.

13 A reporting entity need not have exercised its power to direct the activities of an entity to control that entity. A reporting entity can have power even if, for example, it has not exercised its voting rights or options to acquire voting rights, or is not actively directing the activities of another entity.

Returns

14 The proposed definition retains the concept in FRS 27 that control conveys the right to obtain benefits from another entity. The exposure draft uses the term 'returns' rather than 'benefits', as used in FRS 27, because many interpret 'benefits' to imply only positive returns. It believes that 'returns' makes more explicit that a reporting entity may obtain positive or negative returns.

15 Paragraphs 4–11 of the draft FRS set out its proposals regarding the definition of control. It sets out its reasoning for those proposals in paragraphs BC32–BC62 of the Basis for Conclusions.

Question 1

Do you think that the proposed control definition could be applied to all entities within the scope of FRS 27 as well as those within the scope of INT FRS 12? If not, what are the application difficulties?

Question 2

Is the control principle as articulated in the draft FRS an appropriate basis for consolidation?

Assessing control

16 The exposure draft retains the presumption in FRS 27 that a reporting entity that can exercise

more than half of the voting rights in another entity has power to direct the activities in the absence of circumstances that indicate otherwise. The exposure draft provides guidance on how to assess power and returns when:

- (a) a reporting entity has less than a majority of the voting rights.
- (b) assessing control of a structured entity.

Power without a majority of the voting rights

- 17 The exposure draft clarifies its view that a reporting entity that holds less than half of the voting rights in another entity can control that other entity in some situations. The exposure draft includes application guidance on how to apply the control principle when assessing whether a reporting entity has power to direct the activities of another entity with less than half of the voting rights. This guidance also considers:
- (a) options and convertible instruments to obtain voting rights of an entity.
 - (b) how to assess whether an entity has control if it holds voting rights both directly and on behalf of other parties as an agent.
- 18 Paragraphs 26–29 and B9–B16 of the draft FRS set out its proposals regarding the assessment of power with less than half of the voting rights. It sets out its reasoning for those proposals in paragraphs BC63–BC97 of the Basis for Conclusions.

Question 3

Are the requirements and guidance regarding the assessment of control sufficient to enable the consistent application of the control definition? If not, why not? What additional guidance is needed or what guidance should be removed?

Question 4

Do you agree with its proposals regarding options and convertible instruments when assessing control of an entity? If not, please describe in what situations, if any, you think that options or convertible instruments would give the option holder the power to direct the activities of an entity.

Question 5

Do you agree with its proposals for situations in which a party holds voting rights both directly and on behalf of other parties as an agent? If not, please describe the circumstances in which the proposals would lead to an inappropriate consolidation outcome.

Structured entities

- 19 The exposure draft introduces the term ‘structured entity’. Special purpose entities referred to in INT FRS 12 have characteristics similar to structured entities.
- 20 Paragraphs 30–38 of the draft FRS contain guidance on assessing control of a structured entity. Unlike entities that are controlled through a governing body there is no single, simple test that it could identify for assessing control of a structured entity. Rather, the exposure draft proposes that a reporting entity should assess the particular circumstances of its relationship with a structured entity, and consider factors such as the purpose and design of the structured entity and how decisions are made about the activities that cause the returns of the entity to vary. It sets out its reasoning for the proposals for structured entities in paragraphs BC98–BC121 of the Basis for Conclusions.

- 21 For the reasons set out in paragraph BC112, power can be difficult to assess when considering who controls a structured entity. Some think that power could be easily disguised and, therefore, that a reporting entity might more easily avoid consolidating a structured entity that it controls than would be the case in accordance with INT FRS 12. One way of addressing this would be to propose a risks and rewards 'fall back' test if power cannot be assessed. According to that approach, a reporting entity would consolidate another entity if it is exposed to a particular level of variability of returns of a structured entity, without any requirement to have the power to direct the activities of that structured entity. Others think that consolidation on the basis of control creates fewer structuring opportunities than control with a 'fall back' test. They are concerned that a 'fall back' test creates an incentive to deliberately shift the basis of consolidation away from control.

Question 6

Do you agree with the definition of a structured entity in paragraph 30 of the draft FRS? If not, how would you describe or define such an entity?

Question 7

Are the requirements and guidance regarding the assessment of control of a structured entity in paragraphs 30–38 of the draft FRS sufficient to enable consistent application of the control definition? If not, why not? What additional guidance is needed?

Question 8

Should the FRS on consolidated financial statements include a risks and rewards 'fall back' test? If so, what level of variability of returns should be the basis for the test and why? Please state how you would calculate the variability of returns and why you believe it is appropriate to have an exception to the principle that consolidation is on the basis of control.

Disclosure

- 22 The exposure draft proposes enhanced disclosure requirements for consolidated entities, particularly relating to the effect of non-controlling interests.
- 23 In addition, the global financial crisis has highlighted a need for better disclosure about the nature of, and risks associated with, a reporting entity's involvement with structured entities that the reporting entity does not control. Such disclosure is often referred to as information about 'off balance sheet' activities. Therefore, the exposure draft proposes requiring a reporting entity to disclose:
- (a) information about the basis of control and the related accounting consequences.
 - (b) information about the interest that the non-controlling interests have in the group's activities.
 - (c) information about restrictions on assets and liabilities held in subsidiaries, including the claims of non-controlling interests.
 - (d) information about unconsolidated structured entities that the reporting entity does not control, but with which the reporting entity has involvement.
- 24 Paragraphs 48–50 and B30–B49 of the draft FRS set out the proposed disclosure requirements. It sets out its reasoning for those proposals in paragraphs BC122–BC145 of the Basis for Conclusions.

Question 9

Do the proposed disclosure requirements described in paragraph 23 provide decision-useful information? Please identify any disclosure requirements that you think should be removed from, or added to, the draft FRS.

Question 10

Do you think that reporting entities will, or should, have available the information to meet the disclosure requirements? Please identify those requirements with which you believe it will be difficult for reporting entities to comply, or that are likely to impose significant costs on reporting entities.

Other matters

Reputational risk

- 25 In the context of the exposure draft, reputational risk refers to a reporting entity's implicit commitment to provide support to unconsolidated structured entities without having a contractual or constructive obligation to do so. In response to questions raised as a result of the global financial crisis, it considered whether reputational risk should be a basis for consolidation.
- 26 It concluded that reputational risk is not an appropriate basis for consolidation. However, the exposure draft proposes that a reporting entity should be required to disclose that it has provided support to unconsolidated structured entities despite not having a contractual or constructive obligation to do so.

Question 11

- (a) Do you think that reputational risk is an appropriate basis for consolidation? If so, please describe how it meets the definition of control and how such a basis of consolidation might work in practice.
- (b) Do you think that the proposed disclosures in paragraph B47 are sufficient? If not, how should they be enhanced?

Accounting for associates and the equity method

- 27 The exposure draft reaffirms that a group is a parent and all its subsidiaries. Associates, as defined in FRS 28 *Investments in Associates*, are not part of the group. Yet the equity method in FRS 28 treats an associate as if it were part of the group because it requires an entity to make consolidating adjustments for associates similar to those required for subsidiaries. For example, the equity method requires elimination of profits and losses resulting from transactions between an investor and its associates.
- 28 Some argue that the equity method is not a consolidation method but a measurement method for investments in entities that are outside the group. However, if the equity method represents a measurement method only, it is unclear why the equity method requires consolidating procedures. Respondents to ED 9 *Joint Arrangements* have noted these issues.
- 29 When the concept of significant influence in FRS 28 was developed it was in the context of a consolidation requirement that focused on who has a majority of the voting rights. There was a clear need to address the circumstances in which a reporting entity had involvement with an entity beyond that of a passive investor.

- 30 The consolidation model in FRSs has developed well beyond a simple voting rights model. FRS 27 has a focus on control of the strategic operating and financing policies and identifies circumstances in which other factors override voting rights. The proposals in this exposure draft go even further by focusing on the different ways that a reporting entity might have power to direct the activities of another entity. The disclosures proposed are intended to assist investors and other users in assessing the risks to which the reporting entity is exposed as a consequence of its involvement with entities that the reporting entity does not control.
- 31 Despite the improvements to the consolidation model, the concept of significant influence has not been deliberated by it. During its deliberations on consolidation it noted the overlap, and possible conflict, between the proposals in the exposure draft and the requirements in FRS 28.
- 32 The issues identified in FRS 28 raise the question of whether it should consider the definition of significant influence and the use of the equity method in FRS 28. It noted that consideration of the requirements in FRS 28, together with the proposals in this exposure draft and the concurrent development of a replacement for FRS 31 *Interests in Joint Ventures*, would permit the development of a cohesive set of requirements for all investments in entities.

Question 12

Do you think that it should consider the definition of significant influence and the use of the equity method with a view to developing proposals as part of a separate project that might address the concerns raised relating to FRS 28?

[Draft] Financial Reporting Standard X *Consolidated Financial Statements* ([draft] FRS X) is set out in paragraphs 1–54 and Appendices A–C. All the paragraphs have equal authority. Paragraphs in **bold type** state the main principles. Terms defined in Appendix A are in *italics* the first time they appear in the [draft] FRS. Definitions of other terms are given in the Glossary for Financial Reporting Standards. [Draft] FRS X should be read in the context of its core principle and the Basis for Conclusions, the *Preface to Financial Reporting Standards* and the *Framework for the Preparation and Presentation of Financial Statements*. FRS 8 *Accounting Policies, Changes in Accounting Estimates and Errors* provides a basis for selecting and applying accounting policies in the absence of explicit guidance.

[Draft] Financial Reporting Standard X

Consolidated Financial Statements

Core principle

- 1 **A reporting entity presents financial statements that consolidate its assets, liabilities, equity, income, expenses and cash flows with those of the entities that it controls.**

Scope

- 2 This [draft] FRS applies to all entities, except as follows:
- (a) a *parent* need not present *consolidated financial statements* if it meets all of the following conditions:
 - (i) the parent is a wholly-owned *subsidiary* or is a partially-owned subsidiary of another entity and its other owners, including those not otherwise entitled to vote, have been informed about, and do not object to, the parent not presenting consolidated financial statements;
 - (ii) the parent's debt or equity instruments are not traded in a public market (a domestic or foreign stock exchange or an over-the-counter market, including local and regional markets);
 - (iii) the parent did not file, nor is it in the process of filing, its financial statements with a securities commission or other regulatory organisation for the purpose of issuing any class of instruments in a public market; and
 - (iv) the ultimate or any intermediate parent of the parent produces consolidated financial statements available for public use that comply with FRSs.
 - (b) this [draft] FRS does not apply to post-employment benefit plans or other long-term employee benefit plans to which FRS 19 *Employee Benefits* applies.
- 3 This [draft] FRS does not deal with the accounting for business combinations and its effect on consolidation, including goodwill arising on a business combination (for which see FRS 103 *Business Combinations*).

Control of an entity

- 4 **A reporting entity controls another entity when the reporting entity has the power to direct the activities of that other entity to generate returns for the reporting entity.**
- 5 A parent does not share control of a subsidiary. The parent's power to direct the activities of a subsidiary precludes others from controlling the subsidiary.
- 6 Although a parent does not share control of a subsidiary, its power need not be absolute. *Protective rights* held by other parties do not preclude a parent from controlling a subsidiary but might restrict its power. Paragraphs B1 and B2 provide additional guidance on protective rights.
- 7 Although a parent has the power to direct the activities of a subsidiary to generate returns for its own benefit, other parties, including *non-controlling interests*, can share those returns.

Power to direct the activities

- 8 A reporting entity can possess the power to direct the activities of another entity by different

means, including by having voting rights, by having options or convertible instruments to obtain voting rights, by means of contractual arrangements, or a combination of these. A reporting entity need not have exercised its power to direct the activities of an entity to control that entity.

- 9 A reporting entity can have power by having an agent act on its behalf. In contrast, a reporting entity does not have power when it is acting solely as an agent. Paragraphs B3–B8 provide guidance on the relationship between a principal and its agent.

Returns*

- 10 *Returns from involvement with an entity* vary with that entity's activities and can be positive or negative.
- 11 A parent is exposed to the variability of returns and has the ability to affect the returns generated for it. Returns generated for a parent can include:
- (a) dividends, other forms of economic benefits distributed by a subsidiary, and changes in the value of the subsidiary attributable to the parent and any of the parent's other subsidiaries.
 - (b) upfront fees, access to cash or fees for servicing a subsidiary's assets or liabilities, fees and exposure to loss from providing credit or liquidity support, residual interests in the subsidiary's assets and liabilities on liquidation of that subsidiary, tax benefits, and access to liquidity that a parent has from controlling a subsidiary.
 - (c) returns that are not available to non-controlling interests. For example, a parent might use its own assets (including assets of its other subsidiaries) in combination with the assets of a subsidiary, such as combining functions to achieve economies of scale, sourcing scarce products, gaining access to proprietary knowledge or limiting some operations or assets, to enhance the value of the parent's other assets.
 - (d) cost savings or a reduction in expenses.

Assessing control

- 12 **When assessing control, a reporting entity shall consider power and returns together, and how the reporting entity can use its power to affect the returns.**
- 13 A reporting entity's power to direct the activities of another entity is generally correlated with its exposure to the variability of returns from that other entity.
- 14 A reporting entity shall consider all relevant facts and circumstances when assessing control.

Assessment is continuous

- 15 **A reporting entity shall assess control continuously.**
- 16 A reporting entity's power to direct the activities of another entity can change as a consequence of actions by the reporting entity or because of changes in facts and circumstances. Fluctuations in the reporting entity's returns, without a change in the reporting entity's power to direct the activities of another entity, does not cause that reporting entity to obtain or lose control of that other entity. However, if the reporting entity ceases to receive returns from its involvement with an entity, it does not control that entity.

Related arrangements

* Note for readers of the exposure draft. The term 'returns', as used in this draft FRS, replaces the term 'benefits' used in FRS 27 *Consolidated and Separate Financial Statements*, which the proposed FRS revises.

17 A reporting entity shall consider the terms and conditions of all related arrangements when assessing control.

18 One or more of the following indicate that a reporting entity should treat multiple arrangements as related when assessing control:

- (a) The arrangements are entered into at the same time or in contemplation of each other.
- (b) The arrangements form a single arrangement designed to achieve an overall commercial effect.
- (c) One arrangement considered on its own is not justified economically, but it is justified economically when considered together with other arrangements.

Assessing returns

19 The returns generated for a reporting entity are returns it receives from its involvement with another entity, including returns from related arrangements.

20 A reporting entity's returns can include fixed fees in conjunction with variable returns from related arrangements, and include returns already received as well as those to be received. For example, if a reporting entity receives an initial fixed fee for sponsoring an entity and, as a result of a related arrangement, provides credit and liquidity support, the initial fixed fee and the returns (both positive and negative) relating to the credit and liquidity support are considered together.

Assessing power to direct activities

21 A reporting entity shall assess whether it has power to direct the activities:

- (a) of an entity by having voting rights or other arrangements (see paragraphs 23–29).
- (b) of a *structured entity* (see paragraphs 30–38).

22 A reporting entity has the power to direct the activities of another entity if it can determine that other entity's strategic operating and financing policies.

Power to direct activities with a majority of the voting rights

23 A reporting entity can have the power to direct the activities of another entity by having the power to appoint or remove the members of that entity's governing body that have more than half of the voting rights within that body, if the determination of strategic operating and financing policies is by that body.

24 If the appointment or removal of the members of an entity's governing body is determined by voting rights, a reporting entity with more than half of those voting rights controls that governing body and has the power to direct the activities of that entity unless paragraph 25 applies.

Majority of the voting rights but no power to direct activities

25 A reporting entity with more than half of the voting rights of another entity might not have the power to direct the activities of that other entity. This situation will exist if legal requirements, the founding documents of the other entity or other contractual arrangements restrict the power of the reporting entity to the extent that it does not have the power to direct the activities of the entity, or if another *party* has the power to direct the activities of the entity.

For example, if an entity in which a reporting entity has more than half of the voting rights is placed under legal supervision, the reporting entity is prevented from having the power to direct the activities of that entity and does not control that entity.

Power to direct activities without a majority of the voting rights

- 26 A reporting entity can have the power to direct the activities of another entity even if it holds less than half of the voting rights of that entity.
- 27 A reporting entity with less than half of the voting rights has the power to direct the activities of another entity if:
- (a) the reporting entity has more voting rights than any other party; and
 - (b) the reporting entity's voting rights are sufficient to give the reporting entity the ability to determine the entity's strategic operating and financing policies.
- 28 For example, a reporting entity can have the power to direct the activities of another entity if the reporting entity is the dominant shareholder that holds voting rights and all the other shareholders with voting rights are widely dispersed and are not organised in such a way that they actively co-operate when they exercise their votes so as to have more voting power than the reporting entity.
- 29 A reporting entity can also have the power to direct the activities of another entity by means of other arrangements. Paragraphs B9–B16 provide application guidance for circumstances in which a reporting entity has the power to direct the activities of another entity even though it holds less than half of the voting rights of the entity.

Structured entities

- 30 A structured entity is an entity whose activities are restricted to the extent that those activities are not directed as described in paragraphs 23–29.
- 31 When assessing control of a structured entity, it is necessary to identify how returns from the entity's activities are shared and how decisions, if any, are made about the activities that affect those returns. A reporting entity shall consider all relevant facts and circumstances, including the following:
- (a) the purpose and design of the structured entity (see paragraph 32)
 - (b) the reporting entity's returns from its involvement with the structured entity (see paragraph 33)
 - (c) the activities of the structured entity, including the extent to which the strategic operating and financing policies that direct those activities have been predetermined (see paragraphs 34–36)
 - (d) related arrangements (see paragraph 37)
 - (e) the reporting entity's ability to change the restrictions or predetermined strategic operating and financing policies (see paragraph 38)
 - (f) whether the reporting entity acts as an agent for other parties, or another party acts as its agent (see paragraphs B3–B8).

Purpose and design

- 32 Understanding the purpose and design of a structured entity helps assess how the activities of that entity are directed and how returns are shared among its participants. For example, a

reporting entity is likely to control a structured entity that has been created to undertake activities that are part of the reporting entity's ongoing activities (eg the entity might have been created to hold legal title to an asset that the reporting entity uses in its own activities, providing a source of financing for the reporting entity). The reporting entity is unlikely to surrender power to direct such a structured entity's activities because of the importance of those activities to the reporting entity's activities.

Returns

- 33 Generally, the more a reporting entity is exposed to the variability of returns from its involvement with an entity, the more power the reporting entity is likely to have to direct the activities of that entity that cause the returns to vary. A reporting entity is likely to have power to direct the activities of a structured entity if it is exposed to the variability of returns that are potentially significant to the structured entity and the reporting entity's exposure is more than that of any other party.

Activities

- 34 Control of an entity that has a limited range of activities, such as an entity that manages an asset securitisation, is determined on the basis of how that limited range of activities is directed and how the returns it receives from its involvement with the entity are shared. A reporting entity identifies what activities cause the returns to vary and assesses whether it has power to direct those activities. A reporting entity's ability to act when circumstances arise or events happen constitutes power if that ability relates to the activities that cause the reporting entity's returns to vary. A reporting entity does not have to exercise its power in order to have power to direct the activities of a structured entity.
- 35 For example, if the only assets of an entity are receivables, then managing any defaulting receivables is the only activity that causes the returns to vary and, thus, affects the returns of the structured entity's participants. In this example, the party with the power to direct how any defaulting receivables are managed, and in having that power can affect its returns from its involvement with the entity, controls that entity. A party has that power by managing any defaulting receivables itself or by delegating to its agent the management of defaulting receivables. That party has the power to direct the activities of the entity irrespective of whether any of the receivables actually defaults.
- 36 Sometimes some activities of a structured entity are directed by means of predetermined strategic operating and financing policies that specify the actions that must be taken in response to anticipated events or circumstances. Such predetermined policies can give a reporting entity the power to direct those activities. Those policies are often, although not always, implemented by an agent of the party with the power to direct those activities (see paragraphs B3–B8).

Related arrangements

- 37 A reporting entity can control a structured entity by means of related arrangements (see paragraphs 17 and 18). For example, a reporting entity could establish a structured entity, whose founding documents restrict its activities to purchasing fixed rate receivables of the reporting entity for cash, collecting payments from those receivables and passing those payments to the investors in the structured entity. Receivables that are overdue by more than a specified period are put back to the reporting entity. In this example, in the absence of other facts, the reporting entity controls the structured entity. The entity's founding documents and the put agreement ensure that the reporting entity is exposed to all of the variability of returns generated from the receivables of the structured entity, and has the ability to affect those returns by managing any defaulting receivables. The reporting entity has the power to direct the activities of the structured entity by having the ability to direct how the assets of the structured entity are managed.

Ability to change restrictions or predetermined strategic policies

- 38 A reporting entity can have the power to direct the activities of a structured entity if the reporting entity has the ability to change the restrictions or predetermined strategic operating and financing policies according to which the structured entity operates. For example, a reporting entity can have the power to direct the activities of a structured entity by having the right to dissolve the entity or to change (or veto any changes to) the entity's charter or bylaws. A reporting entity can have the right to dissolve an entity by holding liquidation, redemption or other rights.

Accounting requirements

- 39 **A reporting entity shall present financial statements that consolidate its assets, liabilities, equity, income, expenses and cash flows with those of the entities that it controls and shall present them as those of a single entity.**
- 40 Consolidation of a subsidiary begins from the date when a parent obtains control of the subsidiary and ceases on the date when the parent loses control.
- 41 **A reporting entity shall prepare consolidated financial statements using uniform accounting policies for like transactions and other events in similar circumstances.**
- 42 Paragraphs B17–B21 provide guidance on the preparation of consolidated financial statements.

Non-controlling interests

- 43 A reporting entity presents non-controlling interests in the consolidated statement of financial position within equity, separately from the equity of the owners of the parent.
- 44 Changes in a parent's ownership interest in a subsidiary that do not result in the parent losing control of the subsidiary are equity transactions (ie transactions with owners in their capacity as owners).
- 45 Paragraphs B22–B25 provide guidance on accounting for non-controlling interests in consolidated financial statements.

Loss of control

- 46 If a parent loses control of a subsidiary, the parent:
- (a) derecognises the assets and liabilities of the former subsidiary from the consolidated statement of financial position;
 - (b) recognises the gain or loss associated with the loss of control attributable to the former controlling interest; and
 - (c) accounts for any investment retained in the former subsidiary and any amounts owed by or to the former subsidiary in accordance with other FRSs from the date when control is lost.
- 47 Paragraphs B26–B29 provide guidance on accounting for the loss of control.

Disclosure

- 48 A reporting entity shall disclose information that enables users of its financial statements to evaluate:
- (a) the basis of control and the related accounting consequences;
 - (b) the interest that the non-controlling interests have in the *group's* activities;
 - (c) the nature and financial effect of restrictions that are a consequence of assets and liabilities being held by subsidiaries;
 - (d) the nature of, and risks associated with, the reporting entity's involvement with structured entities that the reporting entity does not control;
 - (e) the accounting consequences of changes in the reporting entity's ownership interest in a subsidiary that do not result in a loss of control; and
 - (f) the accounting consequences when the reporting entity loses control of a subsidiary during the reporting period.
- 49 To meet the objectives in paragraph 48, a reporting entity shall disclose the information specified in paragraphs B30–B49.
- 50 If the specific disclosures required by this and other FRSs do not meet the objectives in paragraph 48, a reporting entity shall disclose whatever additional information is necessary to meet those objectives.

Effective date and transition

Effective date

- 51 A reporting entity shall apply this [draft] FRS prospectively for annual periods beginning on or after [date to be inserted after exposure]. Earlier application is permitted. If a reporting entity applies this [draft] FRS in its financial statements for a period before [date to be inserted after exposure], it shall disclose that fact.

Transition

- 52 When application of the requirements of this [draft] FRS for the first time results in a reporting entity consolidating an entity that was not consolidated in accordance with FRS 27 *Consolidated and Separate Financial Statements* and INT FRS 12 *Consolidation—Special Purpose Entities*, a reporting entity applies the requirements of FRS 103. The date of first applying the [draft] FRS is the deemed acquisition date, unless the acquisition date as defined in FRS 103 is after the date of first applying the [draft] FRS.
- 53 When application of the requirements of this [draft] FRS for the first time results in a reporting entity no longer consolidating an entity that was consolidated in accordance with FRS 27 and INT FRS 12, a reporting entity applies the requirements of the [draft] FRS relating to the loss of control on the date of first applying the [draft] FRS, unless the date of losing control is after the date of first applying the [draft] FRS.

Withdrawal of INT FRS 12

- 54 This [draft] FRS supersedes INT FRS 12 *Consolidation—Special Purpose Entities*.

Appendix A Defined terms

This appendix is an integral part of the [draft] FRS.

consolidated financial statements	The financial statements of a parent and the entities that it controls presented as a single entity.
control of an entity	The power of a reporting entity to direct the activities of another entity to generate returns for the reporting entity.
group	A parent and all its subsidiaries .
involvement with a structured entity	For the purposes of this [draft] FRS, involvement with a structured entity includes both contractual and non-contractual involvement that exposes the reporting entity to variability of returns of the structured entity. Involvement includes the holding of equity or debt instruments, as well as other forms of involvement such as the provision of funding, liquidity support, credit enhancement, guarantees, and asset management services.
non-controlling interest	Equity in a subsidiary not attributable, directly or indirectly, to a parent .
parent	An entity that has one or more subsidiaries .
party	For the purposes of this [draft] FRS, party is used broadly to include legal and other entities as well as a single individual or a group of individuals.
protective rights	Rights of a party relating to the activities of an entity that do not give the party control of the entity , nor do they prevent another party from controlling that entity.
returns from involvement with an entity	Returns that vary with the activities of an entity and can be positive or negative.
structured entity	An entity whose activities are restricted to the extent that those activities are not directed as described in paragraphs 23–29.
subsidiary	An entity that is controlled by a parent . A legal structure such as a company or trust can comprise more than one *entity.

* Note for the readers of the exposure draft. An entity within a legal structure referred to in the definition of a subsidiary is sometimes referred to in national GAAP as a silo.

Appendix B

Application guidance

This appendix is an integral part of the [draft] FRS.

Protective rights

- B1 A reporting entity can control another entity even though other parties have protective rights relating to the activities of that other entity.
- B2 Protective rights are designed to protect the interests of the party holding those rights without giving that party control of the entity to which they relate. They include, for example:
- (a) approval or veto rights granted to other parties that do not affect the strategic operating and financing policies of the entity. Protective rights often apply to fundamental changes in the activities of an entity, or apply only in exceptional circumstances. For example:
 - (i) a lender might have rights that protect the lender from the risk that the entity will change its activities to the detriment of the lender, such as selling important assets or undertaking activities that change the credit risk of the entity.
 - (ii) non-controlling interests might have the right to approve capital expenditure greater than a particular amount, or the right to approve the issue of equity or debt instruments.
 - (b) the ability to remove the party that directs the activities of the entity in circumstances such as bankruptcy or on breach of contract by that party.
 - (c) limitations on the operating activities of an entity. For example, a franchise agreement for which the entity is the franchisee might restrict the pricing, advertising or other operating activities of the entity but would not give the franchisor control of the franchisee. Such rights usually protect the brand of the franchisor.

Agency relationships

- B3 An agent is a party engaged to act on behalf of another party or parties (the principal(s)). An agent might have the ability to direct the activities of an entity, for example by making decisions concerning the operating and financing activities of the entity. However, that ability is governed by agreement, law or fiduciary responsibility that requires the agent to act in the best interests of the principal. The agent must use any decision-making ability delegated to it to generate returns primarily for the principal.

Removal rights

- B4 Removal rights can indicate an agency relationship. A principal often has the right to remove, without cause, an agent that is empowered to direct the activities of an entity for the principal. That unconditional right to remove the agent ensures that the principal has the power to direct the activities of the entity. Rights to remove a party only in circumstances such as bankruptcy or on breach of contract by that party are protective rights.

Remuneration of an agent

- B5 An agent is remunerated for the services it performs by means of a fee that is commensurate with those services. Fees that are not commensurate with the services performed indicate involvement with an entity beyond that of an agent and, therefore, might indicate control.

- B6 Any of the following factors might indicate that fees are not commensurate with the services performed:
- (a) The fees are more than would be received for similar services negotiated on an arm's length basis.
 - (b) The fees are large relative to the total expected returns of the entity to which the services are provided.
 - (c) The expected variability in the fees is large relative to the total expected variability of the returns of the entity to which the services are provided.
- B7 The remuneration of an agent can be a fixed or performance-related fee. If the agent receives a performance-related fee, the agency relationship can be difficult to distinguish from a controlling relationship. This is because the agent can use its ability to direct the activities of the entity to affect its remuneration. However, if this ability is limited by the agent's responsibility to act in the best interests of the principal, the performance-related fee that the agent receives is remuneration for the services it performs and does not indicate involvement with the entity beyond that of an agent.
- B8 A performance-related fee of an agent is often distinguishable from the returns of the investors for whom the agent is acting. For example, an investor in a fund will benefit from increases in the value of the fund and suffer from decreases in the value of the fund. In contrast, an agent might be paid a performance-related fee for a specified period and the agent is unlikely to be required to contribute to the fund (ie refund fees already received) if the value of the fund decreases.

Power to direct activities without a majority of the voting rights

- B9 When assessing control, a reporting entity considers all relevant facts and circumstances, including the following indicators of power to direct the activities of an entity:
- (a) The reporting entity can dominate the governing body, and therefore determine the strategic operating and financing policies. Examples of indicators are:
 - (i) dominating the process of electing members of the entity's governing body or obtaining proxies from other holders of voting interests; and
 - (ii) appointing members to fill vacancies on the entity's governing body until the next election.
 - (b) The reporting entity can appoint, hire, reassign or dismiss the entity's key management personnel.
 - (c) The reporting entity shares resources with the entity. For example, the entity and the reporting entity might have the same members of their governing bodies, or share key management personnel or other staff.
 - (d) The reporting entity has the ability to direct the entity to enter into significant transactions that benefit the reporting entity.
 - (e) The reporting entity has access to the residual assets of the entity, such as:
 - (i) by dissolving the entity and redirecting the use of its assets; or
 - (ii) having access, under a statute or an agreement, to the entity's resources.

Agreement with other vote holders

- B10 An agreement between a reporting entity and other vote holders can give the reporting entity the right to exercise voting rights sufficient to give the reporting entity the power to direct the activities of another entity, even though the reporting entity itself holds voting rights that would not be sufficient to give it power. If the reporting entity can exercise those voting rights to generate returns for itself, the reporting entity controls the other entity to which the voting rights relate.
- B11 Sometimes it can be difficult to identify whether a reporting entity that holds voting rights, both directly and on behalf of other parties as an agent, uses the voting rights of the other parties for its own benefit or for the benefit of those other parties. In such circumstances, in assessing whether it has voting rights sufficient to control another entity, the reporting entity excludes the voting rights it holds as an agent only if the reporting entity can demonstrate that it is obliged to act in the best interests of those other parties or has implemented policies and procedures that ensure the independence of the decision-making in its role as an agent from that as a holder of voting rights directly.

Parties that act for a reporting entity

- B12 The following are examples of parties that often act for a reporting entity:
- (a) the reporting entity's related parties as defined in FRS 24 *Related Party Disclosures*.
 - (b) a party that received its interest in the entity as a contribution from the reporting entity.
 - (c) a party that has agreed not to sell, transfer or encumber its interests in the entity without the prior approval of the reporting entity.
 - (d) a party that cannot finance its operations without financial support from the reporting entity.
 - (e) an entity with the same board of directors as the reporting entity.

Options and convertible instruments

- B13 When assessing control, a reporting entity considers whether its power from holding options or convertible instruments to obtain voting rights, taken in conjunction with other relevant facts and circumstances, gives it the power to direct the activities of another entity. A reporting entity that holds options or convertible instruments has power to direct the activities of another entity if (a), (b) or (c) applies:
- (a) the governing body of that entity determines strategic operating and financing policies in accordance with the wishes of the reporting entity. This might be the if, for example, the reporting entity holds voting rights together with options or convertible instruments to obtain voting rights that, if exercised or converted, would give the reporting entity voting rights sufficient to determine the entity's strategic operating and financing policies.
 - (b) any party with voting rights that is the counterparty to an option agreement acts as an agent for the reporting entity and those voting rights are sufficient to give the reporting entity the ability to determine the entity's strategic operating and financing policies.
 - (c) the option or conversion agreement gives the reporting entity particular rights relating to the strategic operating and financing policies that enable the reporting entity to have the power to direct the activities of the entity.

Other arrangements

- B14 When assessing control, a reporting entity shall consider what powers it has to direct activities of an entity that arise from arrangements other than those that give the reporting entity voting rights.
- B15 Such arrangements could enable the reporting entity to direct activities that would normally be directed by the governing body of that other entity, such as agreements that give the reporting entity the power to direct the manufacturing processes of an entity, appoint personnel or direct other operating activities.
- B16 Economic dependence of an entity on the reporting entity (such as relations of a supplier to its main customer) does not, by itself, lead to the reporting entity having the power to direct the activities of that other entity. However, the reporting entity might have that power if its other arrangements are considered in conjunction with its voting rights. Sometimes having more voting rights than any other party enables a reporting entity to prevent other parties from changing the contractual arrangements the reporting entity uses to direct the activities of another entity.

Accounting requirements

Consolidation procedures

- B17 Consolidated financial statements:
- (a) combine like items of assets, liabilities, equity, income, expenses and cash flows of the parent and its subsidiaries;
 - (b) offset (eliminate) the carrying amount of the parent's investment in each subsidiary and the parent's portion of equity of each subsidiary (FRS 103 explains how to account for any related goodwill); and
 - (c) eliminate in full intragroup assets and liabilities, equity, income, expenses and cash flows relating to transactions between entities of the group (profits or losses resulting from intragroup transactions that are recognised in assets, such as inventory and fixed assets, are eliminated in full).

Measurement

- B18 A reporting entity includes the income and expenses of a subsidiary in the consolidated financial statements from the acquisition date as defined in FRS 103 until the date when the reporting entity ceases to control the subsidiary. Income and expenses of the subsidiary are based on the amounts of the assets and liabilities recognised in the consolidated financial statements at the acquisition date. For example, depreciation expense recognised in the consolidated statement of comprehensive income after the acquisition date is based on the fair values of the related depreciable assets recognised in the consolidated financial statements at the acquisition date.

Options and convertible instruments

- B19 When a subsidiary has instruments that give other parties an option to obtain equity instruments or to convert a liability into equity instruments, a parent determines the proportions of profit or loss and changes in equity allocated to the parent and non-controlling interests on the basis of current ownership interests. The proportions allocated to the parent and non-controlling interests do not reflect the possible exercise of options or convertible instruments.

Reporting date

- B20 The financial statements of the parent and its subsidiaries used in the preparation of the consolidated financial statements have the same reporting date. When the end of the reporting period of the parent is different from that of a subsidiary, the subsidiary prepares, for consolidation purposes, additional financial statements as of the same date as the financial statements of the parent unless it is impracticable to do so.
- B21 When it is impracticable to do so, the financial statements of a subsidiary used in the preparation of consolidated financial statements are prepared as of a date different from that of the parent's financial statements. The reporting entity makes adjustments for the effects of significant transactions or events that occur between that date and the date of the parent's financial statements. In any case, the difference between the date of the subsidiary's financial statements and that of the parent's financial statements can be no more than three months, and the length of the reporting periods and any difference between the dates of the financial statements must be the same from period to period.

Non-controlling interests

- B22 A reporting entity attributes profit or loss and each component of other comprehensive income to the owners of the parent and to the non-controlling interests. The reporting entity attributes total comprehensive income to the owners of the parent and to the non-controlling interests even if this results in the non-controlling interests having a deficit balance.
- B23 If a subsidiary has outstanding cumulative preference shares that are classified as equity and are held by non-controlling interests, the reporting entity computes its share of profit or loss after adjusting for the dividends on such shares, whether or not such dividends have been declared.
- B24 A reporting entity identifies non-controlling interests in the net assets of subsidiaries separately from the parent's interests in them.

Changes in the proportion held by non-controlling interests

- B25 When the proportion of the equity held by non-controlling interests changes, a reporting entity adjusts the carrying amounts of the controlling and non-controlling interests to reflect the changes in their relative interests in the subsidiary. The reporting entity recognises directly in equity any difference between the amount by which the non-controlling interests are adjusted and the fair value of the consideration paid or received and attributes it to the owners of the parent.

Loss of control

Derecognition

- B26 If a reporting entity loses control of a subsidiary, it:
- (a) derecognises:
 - (i) the assets (including any goodwill) and liabilities of the subsidiary at their carrying amounts at the date when control is lost;
 - (ii) the carrying amount of any non-controlling interests in the former subsidiary at the date when control is lost (including any components of other comprehensive income attributable to them).
 - (b) recognises:

- (i) the fair value of the consideration received, if any, from the transaction, event or circumstances that resulted in the loss of control;
 - (ii) if the transaction that resulted in the loss of control involves a distribution of shares of the subsidiary to owners in their capacity as owners, that distribution; and
 - (iii) any investment retained in the former subsidiary at its fair value at the date when control is lost.
- (c) reclassifies to profit or loss, or transfers directly to retained earnings if required in accordance with other FRSs, the amounts recognised in other comprehensive income in relation to the subsidiary on the basis described in paragraph B27.
- (d) recognises any resulting difference as a gain or loss in profit or loss attributable to the parent.

Other comprehensive income

B27 If a reporting entity loses control of a subsidiary, the reporting entity shall account for all amounts recognised in other comprehensive income in relation to that subsidiary on the same basis as would be required if the reporting entity had directly disposed of the related assets or liabilities. Therefore, if a gain or loss previously recognised in other comprehensive income would be reclassified to profit or loss on the disposal of the related assets or liabilities, the parent reclassifies the gain or loss from equity to profit or loss when it loses control of the subsidiary. For example, if a subsidiary has available-for-sale financial assets and the reporting entity loses control of the subsidiary, the reporting entity shall reclassify to profit or loss the gain or loss previously recognised in other comprehensive income in relation to those assets. Similarly, if a revaluation surplus previously recognised in other comprehensive income would be transferred directly to retained earnings on the disposal of the asset, the reporting entity transfers the revaluation surplus directly to retained earnings when it loses control of the subsidiary.

Investment retained on the loss of control

B28 Paragraph 46 states that on the loss of control of a subsidiary, any investment retained in the former subsidiary and any amounts owed by or to the former subsidiary shall be accounted for in accordance with other FRSs from the date when control is lost.

B29 The fair value of any investment retained in the former subsidiary at the date when control is lost shall be regarded as the fair value on initial recognition of a financial asset in accordance with FRS 39 *Financial Instruments: Recognition and Measurement* or, when appropriate, the cost on initial recognition of an investment in an associate or jointly controlled entity.

Disclosures (application of paragraphs 48–50)

B30 To meet the disclosure objectives in paragraph 48, a reporting entity must disclose the information set out in paragraphs B32–B49.

B31 A reporting entity decides, in the light of its circumstances, how much detail it provides to satisfy the requirements of this [draft] FRS, how much emphasis it places on different aspects of the requirements and how it aggregates information to display the overall picture without combining information with different characteristics. It is necessary to strike a balance between burdening financial statements with excessive detail that may not assist users of financial statements and obscuring important information as a result of too much aggregation. For example, a reporting entity shall not obscure important information by including it among a large amount of insignificant detail. Similarly, a reporting entity shall not disclose information that is so aggregated that it obscures important differences between the types of

involvement or associated risks.

Basis of control (paragraph 48(a))

- B32 To help meet the objective in paragraph 48(a), a reporting entity shall describe the basis for its assessment and any significant assumptions or judgements when the reporting entity has concluded that:
- (a) it controls an entity whose activities are directed through voting rights even though the reporting entity has less than half of that entity's voting rights.
 - (b) it does not control an entity whose activities are directed through voting rights even though the reporting entity is the dominant shareholder with voting rights.
 - (c) it does not control a structured entity from which the reporting entity receives returns that are potentially significant to the structured entity.
- B33 A reporting entity shall disclose, in aggregate in relation to the subsidiaries identified in accordance with paragraph B32(a), information to assist users in evaluating the accounting consequences of its assessment that it controls such entities. Such information might include the amounts in the consolidated financial statements relating to total assets, liabilities, revenue and profit or loss of those subsidiaries.
- B34 A reporting entity shall disclose in aggregate, in relation to the entities identified in paragraph B32(b), information to assist users in evaluating the accounting consequences of its assessment that it does not control such entities. Such information might include total assets, liabilities, revenue and profit or loss of those entities.

The interest that the non-controlling interests have in the group's activities (paragraph 48(b))

- B35 To meet the objective in paragraph 48(b), a reporting entity shall disclose information to enable users to evaluate the interest that the non-controlling interests have in the performance, cash flows and net assets of the group. Such information includes, for example:
- (a) the non-controlling interests' share of the group profit or loss and comprehensive income;
 - (b) the non-controlling interests' proportionate interest in dividends paid by subsidiaries; and
 - (c) the business activity or segment to which the non-controlling interests relate.
- B36 A reporting entity shall disclose the date of the financial statements of a subsidiary when such financial statements are used to prepare consolidated financial statements and are as of a date or for a period that is different from that of the consolidated financial statements. The reason why the subsidiary uses a different date or period shall also be disclosed.

Restrictions on consolidated assets and liabilities (paragraph 48(c))

- B37 To meet the objective in paragraph 48(c), a reporting entity shall disclose the nature of restrictions that are a consequence of assets and liabilities being held by subsidiaries, including:
- (a) the extent to which non-controlling interests can restrict the activities of subsidiaries.
 - (b) legal, contractual and regulatory restrictions, such as:

- (i) those that restrict the ability of subsidiaries to transfer cash to entities within the group; and
 - (ii) guarantees that may restrict dividends being paid to entities within the group.
- (c) the carrying amount in the consolidated financial statements of the assets and liabilities to which those restrictions apply.

Involvement with unconsolidated structured entities and associated risks (paragraph 48(d))

- B38 To achieve the disclosure objective in paragraph 48(d), a reporting entity shall disclose information that enables users of its financial statements to evaluate:
- (a) the nature and extent of the reporting entity's involvement with structured entities that it does not control;
 - (b) the nature and extent of, and changes in, the market risk (interest rate, prepayment, currency and other price risk), credit risk and liquidity risk from the reporting entity's involvement with structured entities that it does not control. This exposure may arise from both contractual and non-contractual commitments, and from past and present activities.
- B39 If obtaining any of the information for the disclosures required by this [draft] FRS is impracticable, the reporting entity shall disclose why it is impracticable to obtain the information, and how it manages its exposure to risk from its involvement with unconsolidated structured entities for which it is impracticable to obtain the information.

Nature and extent of involvement (paragraph B38(a))

- B40 In accordance with the disclosure objective in paragraph B38(a), a reporting entity shall disclose information about its involvement with unconsolidated structured entities that the reporting entity set up or sponsored, or with which it has involvement at the date of the consolidated financial statements. This includes summary information about the nature, purpose and activities of the structured entities.

Structured entities set up or sponsored

- B41 A reporting entity shall disclose for unconsolidated structured entities that the reporting entity has set up or sponsored, in tabular format, unless another format is more appropriate, a summary of:
- (a) income from the reporting entity's involvement with structured entities, including a description of the types of income presented in the summary; and
 - (b) the value of assets transferred to those structured entities, at the date the transfers were made.

The summary shall separate the activity into relevant categories (such as by type of structured entity or asset that exposes the reporting entity to different risks). The reporting entity shall also identify the extent to which the activity relates to structured entities with which the reporting entity has involvement at the date of the consolidated financial statements and those with which the reporting entity has none.

- B42 A reporting entity shall disclose the information in paragraph B41 for the current reporting period and the preceding two reporting periods. A reporting entity shall assess whether this information meets the disclosure objective in paragraph B38(a), and provide comparative information for additional reporting periods if that information is necessary to meet the objective.

Nature of risks (paragraph B38(b))

- B43 To achieve the disclosure objective in paragraph B38(b), a reporting entity shall disclose information about its exposure to risks from its involvement with unconsolidated structured entities. The disclosure requirements in paragraphs B44–B47 supplement the disclosure requirements in FRS 107 *Financial Instruments: Disclosures*.
- B44 A reporting entity shall present in tabular format, unless another format is more appropriate, a summary of:
- (a) the carrying amount of the assets and liabilities recognised in the reporting entity's consolidated financial statements relating to the reporting entity's involvement with structured entities.
 - (b) the line items in the consolidated statement of financial position in which those assets and liabilities are recognised.
 - (c) the reported amount of assets held by structured entities with which the entity has involvement, measured at the date of the reporting entity's consolidated financial statements. The reporting entity shall disclose the measurement basis of the assets presented in the summary, distinguishing between assets originated by the reporting entity and those originated by other entities.
 - (d) the amount that best represents the reporting entity's maximum exposure to loss from its involvement with structured entities, including how the maximum exposure to loss is determined.
- B45 The information required in paragraph B44 should be classified into categories that are representative of a reporting entity's exposure to risk (such as by type of structured entity or type of asset).
- B46 In addition, a reporting entity shall disclose other information that is relevant to an assessment of the risks to which the reporting entity is exposed. That other information might include any of the following:
- (a) in relation to structured entities' assets, their categories and credit rating, their weighted-average life, and whether any assets have been written down or downgraded by rating agencies.
 - (b) in relation to funding and loss exposure:
 - (i) the forms of structured entities' funding (eg commercial paper, medium-term notes) and their weighted-average life. That information might include maturity analyses of the assets and funding of structured entities if the structured entities have longer-term assets funded by shorter-term funding.
 - (ii) any difficulties structured entities have experienced in financing their activities during the reporting period.
 - (iii) losses incurred by the reporting entity during the reporting period relating to its involvement with structured entities.
 - (iv) estimated exposure to loss or range of outcomes of that loss that were reasonably possible at the date of the reporting entity's consolidated financial statements, if the reporting entity believes that the maximum exposure to loss is not representative of the estimated exposure to loss. The reporting entity shall explain the methodology used to determine the estimated exposure to loss or range of that loss.

- (v) whether the reporting entity is required to bear any losses before other investors in the structured entity, the ranking and amounts of losses borne by each category of party involved, and the maximum limit of such losses.
- (c) the types of returns the reporting entity received during the reporting period from the financial instruments it holds in structured entities.
- (d) the nature and terms of any obligation of the reporting entity to provide liquidity support to structured entities (eg to purchase assets or commercial paper of the structured entity), including:
 - (i) a description of any triggers associated with the obligation.
 - (ii) whether there are any terms that would limit the obligation.
 - (iii) whether there are any other parties that provide liquidity support and, if so, how the reporting entity's obligation ranks with those other parties.
- (e) in relation to support that has been provided by a reporting entity to structured entities during the reporting period whether:
 - (i) the reporting entity purchased any debt or equity interests in structured entities, and whether any agreement required the reporting entity to make these purchases.
 - (ii) other assistance was provided to structured entities in obtaining any other type of support.
 - (iii) there are any current intentions to provide support or other assistance to structured entities in obtaining any other type of support.

B47 If, during the reporting period, a reporting entity has, without having a contractual or constructive obligation to do so, provided support to structured entities that were not consolidated at the time of providing the support, it shall disclose:

- (a) the extent of support provided, including its nature and amount, including situations in which the reporting entity assisted the structured entity in obtaining another type of support, or in which there are current intentions to do so;
- (b) an explanation of why the support was provided;
- (c) an explanation of how the provision of the support resulted in the reporting entity controlling the structured entity, if applicable.

Accounting consequences of changes in a reporting entity's ownership interest without loss of control (paragraph 48(e))

B48 To meet the objective in paragraph 48(e), a reporting entity shall disclose a schedule that shows the effects on the equity attributable to the owners of the parent of any changes in the ownership interest of the parent in a subsidiary that do not result in a loss of control.

Accounting consequences when a reporting entity loses control of a subsidiary (paragraph 48(f))

B49 To meet the objective in paragraph 48(f), a reporting entity shall disclose the gain or loss, if any, recognised in accordance with paragraph 46, and:

- (a) the portion of that gain or loss attributable to recognising any investment retained in the former subsidiary at its fair value at the date when control is lost; and

- (b) the line item(s) in the statement of comprehensive income in which the gain or loss is recognised (if not presented separately in the statement of comprehensive income).

Appendix C

Amendments to other FRSs

The amendments in this [draft] appendix shall be applied for annual periods beginning on or after [date to be inserted after exposure]. If an entity applies this [draft] FRS for an earlier period, these amendments shall be applied for that earlier period. Amended paragraphs are shown with new text underlined and deleted text struck through.

C1 In Financial Reporting Standards (including Interpretations) applicable at [date to be inserted after exposure], the following references are amended as described below, unless otherwise stated in this appendix.

- References to the current version of INT FRS 12 *Consolidation—Special Purpose Entities* are amended to [draft] FRS X *Consolidated Financial Statements*.
- References to ‘special purpose entity (entities)’ are amended to ‘structured entity (entities)’.

FRS 101 *First-time Adoption of Financial Reporting Standards*

C2 In FRS 101, paragraphs B7 and C1 are amended as follows.

B7 A first-time adopter shall apply the following requirements of ~~FRS 27 (as amended in 2008)~~ [draft] FRS X *Consolidated Financial Statements* prospectively from the date of transition to FRSs:

- (a) the requirement in paragraph ~~28~~ B22 that total comprehensive income is attributed to the owners of the parent and to the non-controlling interests even if this results in the non-controlling interests having a deficit balance;
- (b) the requirements in paragraphs ~~30 and 31~~ B25 for accounting for changes in the parent’s ownership interest in a subsidiary that do not result in a loss of control; and
- (c) the requirements in paragraphs ~~34–37~~ B26–B29 for accounting for a loss of control over a subsidiary, and the related requirements of paragraph 8A of FRS 105 *Non-current Assets Held for Sale and Discontinued Operations*.

However, if a first-time adopter elects to apply FRS 103 (as revised in 2008) retrospectively to past business combinations, it also shall apply ~~FRS 27 (as amended in 2008)~~ [draft] FRS X in accordance with paragraph C1 of this FRS.

C1 A first-time adopter may elect not to apply FRS 103 (as amended in 2008) retrospectively to past business combinations (business combinations that occurred before the date of transition to FRSs). However, if a first-time adopter restates any business combination to comply with FRS 103 (as amended in 2008), it shall restate all later business combinations and shall also apply ~~FRS 27 (as amended in 2008)~~ [draft] FRS X from that same date. For example, if a first-time adopter elects to restate a business combination that occurred on 30 June 20X6, it shall restate all business combinations that occurred between 30 June 20X6 and the date of transition to FRSs, and it shall also apply ~~FRS 27 (amended 2008)~~ [draft] FRS X from 30 June 20X6.

FRS 103 *Business Combinations (as revised in 2008)*

C3 In FRS 103, paragraphs IN2 and 7, Appendix A and paragraphs B13 and B63(e) are amended as follows.

IN2 The second phase of the project addressed the guidance for applying the acquisition

method. Its decided that a significant improvement could be made to financial reporting if they had similar standards for accounting for business combinations. Thus, they decided to conduct the second phase of the project as a joint effort with the objective of reaching the same conclusions. It concluded the second phase of the project by issuing this FRS and FASB Statement No. 141 (revised 2007) *Business Combinations* and the related amendments to FRS 27 *Consolidated and Separate Financial Statements* and FASB Statement No. 160 *Noncontrolling Interests in Consolidated Financial Statements*.*

*In 200X the requirements for consolidated financial statements in FRS 27 were replaced by [draft] FRS X Consolidated Financial Statements.

- 7 The guidance in ~~FRS 27~~ [draft] FRS X Consolidated and Separate Financial Statements shall be used to identify the acquirer—the entity that obtains *control* of the acquiree. If a business combination has occurred but applying the guidance in ~~FRS 27~~ [draft] FRS X does not clearly indicate which of the combining entities is the acquirer, the factors in paragraphs B14–B18 shall be considered in making that determination.

Appendix A (Defined terms)

Control of an entity The power of a reporting entity to ~~govern~~ direct the ~~financial and operating policies~~ activities of another entity ~~so as to obtain benefits from its activities~~ generate returns for the reporting entity.

- B13 The guidance in ~~FRS 27~~ [draft] FRS X Consolidated and Separate Financial Statements shall be used to identify the acquirer—the entity that obtains control of the acquiree. If a business combination has occurred but applying the guidance in ~~FRS 27~~ [draft] FRS X does not clearly indicate which of the combining entities is the acquirer, the factors in paragraphs B14–B18 shall be considered in making that determination.
- B63 Examples of other FRSs that provide guidance on subsequently measuring and accounting for assets acquired and liabilities assumed or incurred in a business combination include:
- (a) ...
- (e) ~~FRS 27~~ [draft] FRS X (as ~~amended in 2008~~) provides guidance on accounting for changes in a parent's ownership interest in a subsidiary after control is obtained.

FRS 107 Financial Instruments: Disclosures

- C4 In FRS 107, paragraph 3(a) is amended as follows.
- 3 This FRS shall be applied by all entities to all types of financial instruments, except:
- (a) those interests in subsidiaries, associates or joint ventures that are accounted for in accordance with [draft] FRS X Consolidated Financial Statements, ~~FRS 27 Consolidated and Separate Financial Statements~~, FRS 28 *Investments in Associates* or FRS 31 *Interests in Joint Ventures*. ...

FRS 1 Presentation of Financial Statements (as revised in 2007)

- C5 In FRS 1, paragraphs 4 and 124 are amended as follows.
- 4 This Standard does not apply to the structure and content of condensed interim financial statements prepared in accordance with FRS 34 *Interim Financial Reporting*. However, paragraphs 15–35 apply to such financial statements. This Standard applies equally to all entities, including those that present consolidated financial statements and those that present separate financial statements defined in [draft]

FRS X Consolidated Financial Statements and FRS 27 Consolidated and Separate Financial Statements.

- 124 Some of the disclosures made in accordance with paragraph 122 are required by other FRSs. For example, ~~FRS 27~~ [draft] FRS X requires an entity to disclose the ~~reasons why the entity's ownership interest does not constitute control, in respect of an investee that is not a subsidiary even though more than half of its voting or potential voting power is owned directly or indirectly through subsidiaries~~ judgements made by management when reaching decisions about whether it controls other entities and the accounting consequences of those judgements. ...

FRS 7 Statement of Cash Flows

- C6 In FRS 7, paragraph 42B is amended as follows.

- 42B Changes in ownership interests in a subsidiary that do not result in a loss of control, such as the subsequent purchase or sale by a parent of a subsidiary's equity instruments, are accounted for as equity transactions (see ~~FRS 27~~ [draft] FRS X Consolidated and Separate Financial Statements (as amended in 2008)). ...

FRS 21 The Effects of Changes in Foreign Exchange Rates

- C7 In FRS 21, paragraphs IN12, 19, 45 and 46 are amended as follows.

- IN12 The Standard permits an entity to present its financial statements in any currency (or currencies). For this purpose, an entity could be a stand-alone entity, a parent preparing consolidated financial statements in accordance with [draft] FRS X Consolidated Financial Statements or a parent, an investor or a venturer preparing separate financial statements in accordance with ~~FRS 27 Consolidated and Separate Financial Statements.~~

- 19 This Standard also permits a stand-alone entity preparing financial statements or an entity preparing separate financial statements in accordance with ~~FRS 27 Consolidated and Separate Financial Statements~~ to present its financial statements in any currency (or currencies). ...

- 45 The incorporation of the results and financial position of a foreign operation with those of the reporting entity follows normal consolidation procedures, such as the elimination of intragroup balances and intragroup transactions of a subsidiary (see ~~FRS 27~~ [draft] FRS X Consolidated Financial Statements and ~~FRS 31 Interests in Joint Ventures~~). ...

- 46 When the financial statements of a foreign operation are as of a date different from that of the reporting entity, the foreign operation often prepares additional statements as of the same date as the reporting entity's financial statements. When this is not done, ~~FRS 27~~ [draft] FRS X allows the use of a different date provided that the difference is no greater than three months and adjustments are made for the effects of any significant transactions or other events that occur between the different dates. In such a case, the assets and liabilities of the foreign operation are translated at the exchange rate at the end of the reporting period of the foreign operation. Adjustments are made for significant changes in exchange rates up to the end of the reporting period of the reporting entity in accordance with ~~FRS 27~~ [draft] FRS X. ...

FRS 24 Related Party Disclosures

- C8 In FRS 24, paragraphs 3, 5, 9 and 14 are amended as follows.

- 3 This Standard requires disclosure of related party transactions and outstanding balances in the separate financial statements of a parent, venturer**

or investor presented in accordance with FRS 27 ~~Consolidated and Separate Financial Statements~~.

5 Related party relationships are a normal feature of commerce and business. For example, entities frequently carry on parts of their activities through subsidiaries, joint ventures and associates. In these circumstances, the entity's ability to affect the strategic financial and operating and financing policies of the investee is through the presence of control, joint control or significant influence.

9 The following terms are used in this Standard with the meanings specified:

Control of an entity is the power of a reporting entity to govern direct the financial and operating policies activities of another entity so as to obtain benefits from its activities generate returns for the reporting entity.

Significant influence is the power to participate in the strategic financial and operating and financing policy decisions of the investee an entity, but is not control over those policies. Significant influence may be gained by share ownership, statute or agreement.

14 The identification of related party relationships between parents and subsidiaries is in addition to the disclosure requirements in FRS 27, ~~[draft] FRS X FRS 28 and FRS 31~~, which require an appropriate listing and description of significant investments in subsidiaries, associates and jointly controlled entities.

FRS 27 ~~Consolidated and Separate Financial Statements~~

C9 In FRS 27, the requirements for consolidated financial statements would be deleted and replaced with FRS X. The accounting and disclosure requirements for separate financial statements would remain in FRS 27; paragraphs would be renumbered, the scope adjusted and editing changes made.

FRS 28 Investments in Associates

C10 In FRS 28, paragraph 8 is deleted and paragraphs IN6, IN8, 2, 5, 9, 12, 13(b), 20 and 35 are amended as follows.

IN6 Furthermore, the Standard provides exemptions from application of the equity method similar to those provided for certain parents not to prepare consolidated financial statements. These exemptions include when the investor is also a parent exempt in accordance with ~~FRS 27 [draft] FRS X Consolidated and Separate Financial Statements~~ from preparing consolidated financial statements (paragraph 13(b)), and when the investor, though not such a parent, can satisfy the same type of conditions that exempt such parents (paragraph 13(c)).

IN8 The Standard clarifies that investments in associates over which the investor has significant influence must be accounted for using the equity method whether or not the investor also has investments in subsidiaries and prepares consolidated financial statements. However, the investor does not apply the equity method when presenting separate financial statements prepared in accordance with FRS 27 Separate Financial Statements.

2 The following terms are used in this Standard with the meanings specified:

Control of an entity is the power of a reporting entity to govern direct the financial and operating policies activities of another entity so as to obtain benefits from its activities generate returns for the reporting entity.

Significant influence is the power to participate in the strategic financial and operating and financing policy decisions of the investee an entity, but is not

control or joint control over those policies.

A subsidiary is an entity, including an unincorporated entity such as a partnership, that is controlled by another entity (known as the parent) a parent.

- 5 Entities that are exempted in accordance with paragraph ~~40 2(a)~~ of ~~FRS 27 [draft] FRS X Consolidated and Separate Financial Statements~~ from consolidation, paragraph 2 of FRS 31 *Interests in Joint Ventures* from applying proportionate consolidation or paragraph 13(c) of this Standard from applying the equity method may present separate financial statements, in accordance with FRS 27 *Separate Financial Statements*, as their only financial statements.
- 9 In assessing ~~whether potential voting rights contribute to~~ significant influence, the entity considers whether its power from holding options or convertible instruments to obtain voting rights, taken in conjunction with other relevant facts and circumstances, gives it the power to participate in the strategic operating and financing policy decisions of an entity. examines all facts and circumstances (including the terms of exercise of the potential voting rights and any other contractual arrangements whether considered individually or in combination) that affect potential rights, except the intention of management and the financial ability to exercise or convert.
- 12 When an investor has instruments that give other parties an option to obtain equity instruments or to convert a liability into equity instruments, When potential voting rights exist, the investor's share of profit or loss of the investee and of changes in the investee's equity is determined on the basis of present ownership interests and does not reflect the possible exercise or conversion of options or convertible instruments potential voting rights.
- 13 **An investment in an associate shall be accounted for using the equity method except when:**
- (a) ...
- (b) **the exception in paragraph ~~40 2(a)~~ of ~~FRS 27 [draft] FRS X~~, allowing a parent that also has an investment in an associate not to present consolidated financial statements, applies; or ...**
- 20 Many of the procedures appropriate for the application of the equity method are similar to the consolidation procedures described in ~~FRS 27 [draft] FRS X~~. Furthermore, ...
- 35 **An investment in an associate shall be accounted for in the investor's separate financial statements in accordance with paragraphs ~~38-43 x-x~~ of FRS 27 (as amended in 200X).**

FRS 31 *Interests in Joint Ventures*

- C11 In FRS 31, paragraphs IN3, IN6, IN9, 2(b), 3, 6, 33, 45 and 46 are amended as follows.
- IN3 For FRS 31 it's main objective was to make the amendments necessary to take account of the extensive changes being made to FRS 27 *Consolidated and Separate Financial Statements** and *Accounting for Investments in Subsidiaries* and FRS 28 *Accounting for Investments in Associates* as part of the Improvements project. ...
- *In 200X the requirements for consolidated financial statements in FRS 27 (as revised in 2003 and amended in 2008) were replaced by [draft] FRS X *Consolidated Financial Statements*.
- IN6 Furthermore, the Standard provides exemptions from application of proportionate consolidation or the equity method similar to those provided for certain parents not to

prepare consolidated financial statements. These exemptions include when the investor is also a parent exempt in accordance with ~~FRS 27~~ [draft] FRS X Consolidated and Separate Financial Statements from preparing consolidated financial statements (paragraph 2(b)), and when the investor, though not such a parent, can satisfy the same type of conditions that exempt such parents (paragraph 2(c)).

IN9 The requirements for the preparation of an investor's separate financial statements are established by reference to FRS 27 Separate Financial Statements.

2 **A venturer with an interest in a jointly controlled entity is exempted from paragraphs 30 (proportionate consolidation) and 38 (equity method) when it meets the following conditions:**

(a) ...

(b) **the exception in paragraph ~~40~~ 2(a) of ~~FRS 27~~ [draft] FRS X Consolidated and Separate Financial Statements allowing a parent that also has an interest in a jointly controlled entity not to present consolidated financial statements is applicable; or ...**

3 **The following terms are used in this Standard with the meanings specified:**

Control of an entity is the power of a reporting entity to govern direct the financial and operating policies activities of another entity so as to obtain benefits from its activities generate returns for the reporting entity.

Significant influence is the power to participate in the strategic financial and operating and financing policy decisions of an economic activity entity, but is not control or joint control over those policies.

6 Entities that are exempted in accordance with paragraph ~~40~~ 2(a) of ~~FRS 27~~ [draft] FRS X from consolidation, paragraph 13(c) of FRS 28 *Investments in Associates* from applying the equity method or paragraph 2 of this Standard from applying proportionate consolidation or the equity method may present separate financial statements as their only financial statements.

33 The application of proportionate consolidation means that the statement of financial position of the venturer includes its share of the assets that it controls jointly and its share of the liabilities for which it is jointly responsible. The statement of comprehensive income of the venturer includes its share of the income and expenses of the jointly controlled entity. Many of the procedures appropriate for the application of proportionate consolidation are similar to the procedures for the consolidation of investments in subsidiaries, which are set out in ~~FRS 27~~ [draft] FRS X.

45 **When an investor ceases to have joint control over an entity, it shall account for any remaining investment in accordance with FRS 39 from that date, provided that the former jointly controlled entity does not become a subsidiary or associate. From the date when a jointly controlled entity becomes a subsidiary of an investor, the investor shall account for its interest in accordance with FRS 27 Separate Financial Statements or [draft] FRS X and FRS 103 *Business Combinations* (as revised in 2008). ...**

46 **An interest in a jointly controlled entity shall be accounted for in a venturer's separate financial statements in accordance with paragraphs ~~38-43~~ x-x of FRS 27 (as amended in 200X).**

FRS 32 *Financial Instruments: Presentation*

C12 In FRS 32, paragraphs 4(a) and AG29 are amended as follows.

4 This Standard shall be applied by all entities to all types of financial instruments except:

- (a) those interests in subsidiaries, associates or joint ventures that are accounted for in accordance with [draft] FRS X Consolidated Financial Statements, ~~FRS 27 Consolidated and Separate Financial Statements~~, ~~FRS 28 Investments in Associates~~ or ~~FRS 31 Interests in Joint Ventures~~. However, ...

AG29 In consolidated financial statements, an entity presents non-controlling interests—ie the interests of other parties in the equity and income of its subsidiaries—in accordance with FRS 1 and ~~FRS 27~~ [draft] FRS X Consolidated Financial Statements. When ...

FRS 33 Earnings per Share

C13 In FRS 33, paragraph 4 is amended as follows.

- 4 When an entity presents both consolidated financial statements and separate financial statements prepared in accordance with [draft] FRS X Consolidated Financial Statements and FRS 27 Consolidated and Separate Financial Statements, respectively, the disclosures required by this Standard need be presented only on the basis of the consolidated information. An ...

FRS 36 Impairment of Assets

C14 In FRS 36, paragraphs IN4 and 4(a) are amended as follows.

IN4 The second phase of the project resulted in the Board issuing simultaneously in 2008 a revised FRS 103 and amendments to ~~FRS 27 Consolidated and Separate Financial Statements*~~. ...

*In 200X the consolidation requirements in FRS 27 were replaced by [draft] FRS X Consolidated Financial Statements.

4 This Standard applies to financial assets classified as:

- (a) subsidiaries, as defined in ~~FRS 27~~ [draft] FRS X Consolidated and Separate Financial Statements; ...

FRS 38 Intangible Assets

C15 In FRS 38, paragraph 3(e) is amended as follows.

3 If another Standard prescribes the accounting for a specific type of intangible asset, an entity applies that Standard instead of this Standard. For example, this Standard does not apply to:

(a) ...

- (e) financial assets as defined in FRS 32. The recognition and measurement of some financial assets are covered by [draft] FRS X Consolidated Financial Statements, ~~FRS 27 Consolidated and Separate Financial Statements~~, ~~FRS 28 Investments in Associates~~ and ~~FRS 31 Interests in Joint Ventures~~.

FRS 39 Financial Instruments: Recognition and Measurement

C16 In FRS 39, paragraphs 2(a) and 15 are amended as follows.

2 This Standard shall be applied by all entities to all types of financial instruments except:

(a) those interests in subsidiaries, associates and joint ventures that are accounted for ~~under~~ in accordance with [draft] FRS X Consolidated Financial Statements, FRS 27 Consolidated and Separate Financial Statements, FRS 28 Investments in Associates or FRS 31 Interests in Joint Ventures. However, ...

15 In consolidated financial statements, paragraphs 16–23 and Appendix A paragraphs AG34–AG52 are applied at a consolidated level. Hence, an entity first consolidates all subsidiaries in accordance with ~~FRS 27 and INT FRS 12 Consolidation—Special Purpose Entities~~ [draft] FRS X Consolidated Financial Statements and then applies paragraphs 16–23 and Appendix A paragraphs AG34–AG52 to the resulting group.

INT FRS 105 *Rights to Interests arising from Decommissioning, Restoration and Environmental Rehabilitation Funds*

C17 In INT FRS 105, paragraph 8 is amended as follows.

8 The contributor shall determine whether it has control, joint control or significant influence over the fund by reference to ~~FRS 27~~ [draft] FRS X Consolidated Financial Statements, FRS 28, and FRS 31 ~~and INT FRS 12~~. If it does, the contributor shall account for its interest in the fund in accordance with those Standards.