

CA Corp Level FRG Sandeepa Pack 05



**JMC JAYASEKERA  
MANAGEMENT CENTRE**  
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## CA – Corporate Level

### SLFRS 11 – Joint Arrangements

Sandeepa Jayasekera

MBA (PIM-SJP), B.Sc. (Acct.) Hons. Gold Medal Winner, ACA, SAT, ACMA (UK), CGMA (UK), CA Prize Winner for AFR subject in Strategic Level II, CA First in Order of Merit Prize Winner in CAB II Level, CIMA Strategic Level Aggregate Prize Winner.

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# What is a Joint Arrangement?

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# Joint Arrangement

Arrangement

2 or More Parties

Jointly Control

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# Requisites to be a Joint Arrangement

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# Joint Arrangement

Contractual Agreement

Joint Control

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# What is Joint Control?

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# Joint Control

Contractually Agreed

To Share the Control

Decisions Require

Unanimous Consent (100%)

of Parties Sharing Control

Contractual Agreement May be a

- Contract
- Minutes of a Discussion
- Articles of the Entity

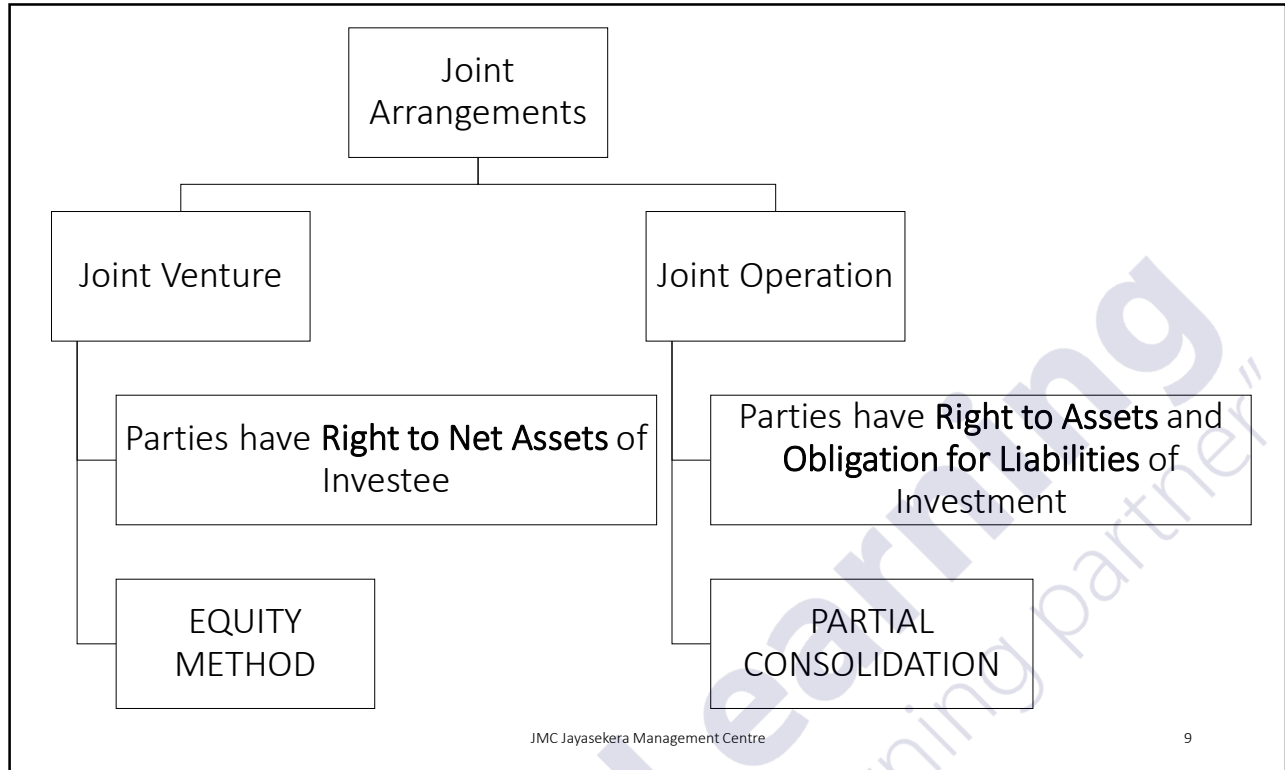
Agreement Generally Include

- Duration
- Capital Contribution
- Sharing Profits and Losses
- Voting Rights
- Appointing Management
- Business Activity

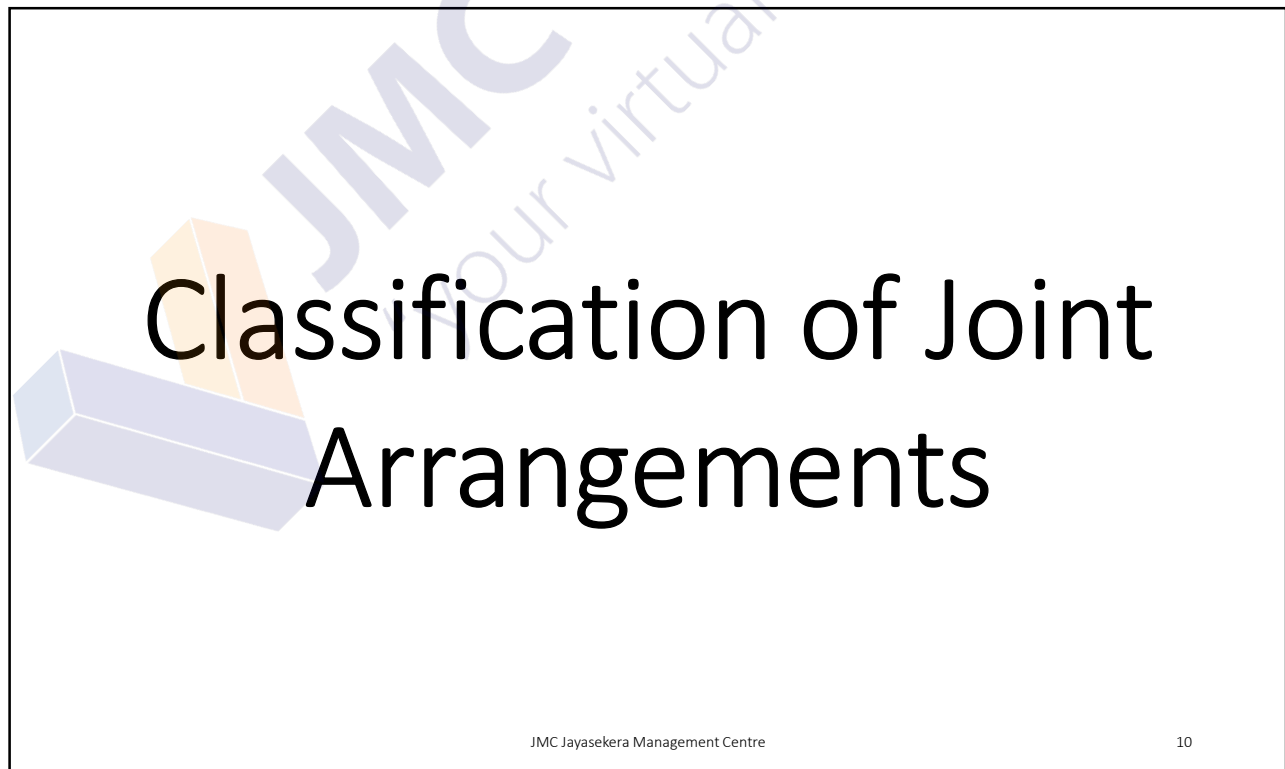
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# Types of Joint Arrangements

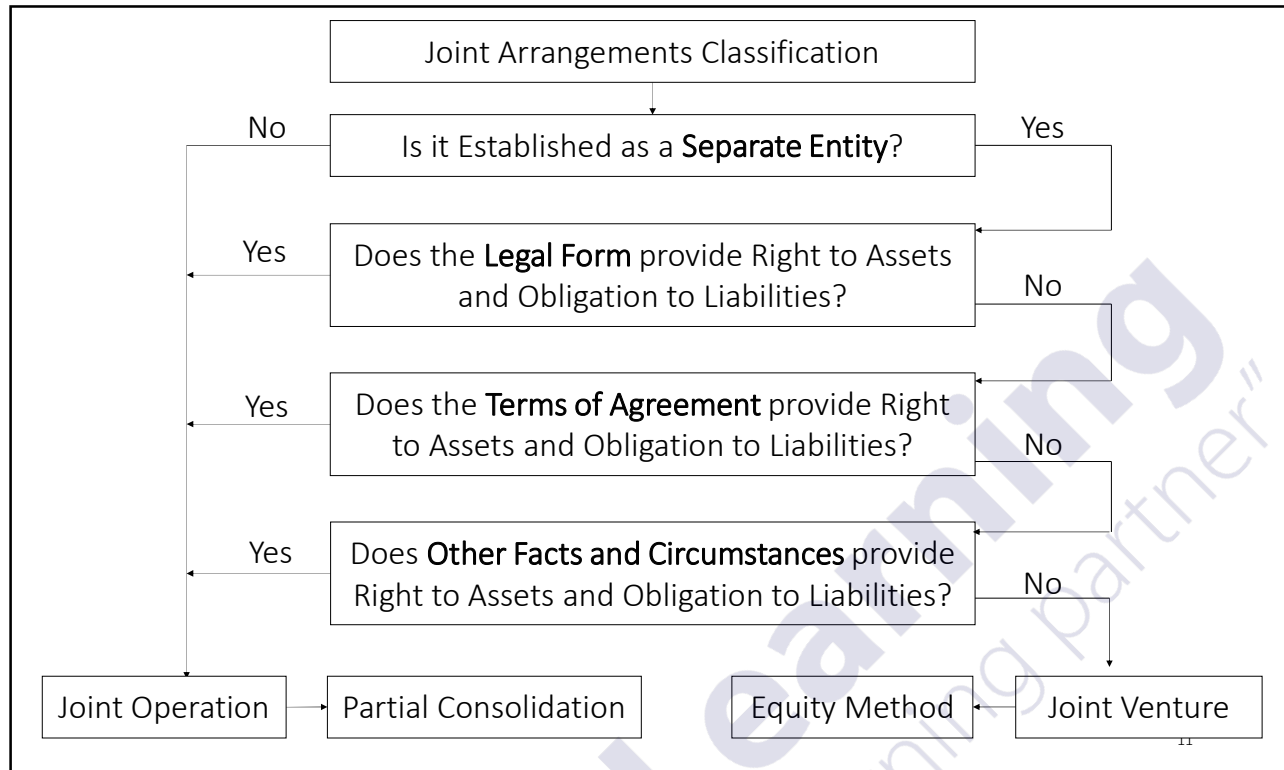
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## Example on Legal Form

- Two parties entered a Joint Arrangement by forming a Company.
- Each party has a 50% ordinary shares.
- The company incorporation has resulted in separating the entity from its owners.
- The assets and liabilities of the company belong to Company, not to the owners.
- Owners are entitling for the Equity (Net Assets)

### Conclusion

Legal form indicates, Parties have rights over net assets. Therefore, it's a Joint Venture

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## Example on Terms of Agreement

- Two parties entered in to a Joint Arrangement by forming a Company.
- Each party has a 50% ordinary shares.
- Owners are entitle for the Equity (Net Assets)
- However, the parties entered in to an agreement
- Agreement Terms says each party has rights over assets and obligation to liabilities in agreed proportions.

### Conclusion

Terms of the Agreement indicates, Parties have rights assets and obligation to liabilities separately. Therefore, it's a Joint Operation.

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## Example on Other Facts and Circumstances

- A and B entered into a Joint Arrangement, and formed company C with 50:50 Ownership.
- Purpose of the Company C is to manufacture a raw material used by A and B
- A and B agreed to Purchase the Output on a 50:50 basis
- A and B has decided the Price of C's product to cover the costs of C.
- C depends on A and B. They have an obligation to provide funds to settle liabilities of C.

### Conclusion

Other Facts and Circumstances Indicate, Parties have rights assets and obligation to liabilities separately. Therefore, it's a Joint Operation.

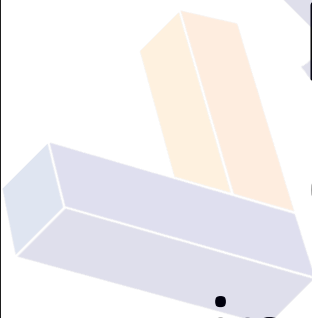
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## Note on Other Facts and Circumstances

Purpose of Joint Arrangement is to Serve Controlling Parties

- E.g. Output of Joint Arrangement is Input of Joint Parties
- E.g. Services Entirely Rendered to Joint Parties

Parties are Settling the Liabilities of Joint Arrangement on a Continuous Basis



## Proportionate Consolidation in Joint Operation



## Line by Line Addition

- Own Assets + Share of Assets held Jointly
- Own Liabilities + Share of Liabilities held Jointly
- Own Revenue + Share of Revenue held Jointly
- Own Expenses + Share of Expenses held Jointly

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## Other Consolidation Adjustments to Share of Investment

- Fair Value of Identifiable Net Assets of Joint Operation
- Acquisition Related Expenses Charged to PnL
- Share of Goodwill or Gain on Bargain Purchase
- Unrealized Gains or Losses
- Goodwill Impairment

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### Question 31

Astro entered into a joint arrangement with Lora to construct the 'Millennium building complex' project on 31 December 2020.

Parties agree to share assets, liabilities and profits on a 50:50 basis.

The decisions required unanimous consent.

The parties had right to assets and obligations to liabilities separately.

The following summarized statements of financial position are provided for Astro and Millennium Project as at 31 December 2020:

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	Astro	Millennium
	Rs 000	Rs 000
Non-current assets	2,300	1,200
Investment in Millenium	525	-
Current assets	575	450
	<b>3,400</b>	<b>1,650</b>
Equity		
Capital (Rs)	2,000	1050
Retained earnings	1,250	-
Current liabilities	150	600
	<b>3,400</b>	<b>1,650</b>

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## Question 31

Required

31.1 Apply SLFRS 11 decide the classification of the investment

31.2 Prepare the financial statements using the relevant accounting treatment.

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## Question 33

*Modified Question from ACCA P2 December 2017*

Fancy is a listed group of companies. The directors currently misunderstand the nature of the control principle. During the year ended 31 March 2018, Fancy entered into a **joint venture** with Loft and established Fred. Fred was structured in such a way that **all business decisions** were taken by the board of directors of **Fancy** and the only decisions which needed the **approval of both** Fancy and Loft were those which were **outside normal** operational decisions.

Fred was financed initially through the issue of **bonds** whose **return** was based upon the **performance** of the joint venture. **Fancy purchased the bonds** from third parties during the year. As a **bondholder**, **Fancy** has the right to **appoint the general manager** of the joint venture.

For the year ended 31 March 2018, Fancy intends to account for Fred under SLFRS 11 Joint Arrangements.

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### Answer 33

According to SLFRS 10 Consolidated Financial Statements, an investor controls an investee when the investor has power over the investee, exposure, or rights, to variable returns from its involvement with the investee and the ability to use its power over the investee to affect the amount of the investor's return.

Fancy makes all of the operational decisions as regards Fred and the only decisions which need the approval of both Fancy and Loft are those which are outside normal operational decisions.

These are **protective rights** for Loft and do not prevent Fancy from having power over Fred.

The concept of returns is quite a broad one and would include a return from the bonds purchased by Fancy in Fred. Hence, Fancy has **exposure to positive and possibly negative returns as the bondholders' return is based upon the performance** of Fred. Fancy is therefore exposed to variable returns from its involvement with Fred. Fancy also has the right to **appoint the general manager** of Fred and thus, together with the operational control exercised by Fancy, this power can be used to affect the amount of the investor's return.

Thus, the conditions set out in SLFRS 10 appear fulfilled, and it can be concluded that Fancy controls Fred. Therefore, Fancy should consolidate Fred as a **subsidiary** in its financial statements as of 31 March 2018.

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### Question 34

*Modified Question from ACCA P2 September 2015*

Universal is involved in the production and trading of natural gas and oil. Universal **jointly owns** an **underground storage** facility with another entity, Galaxy. Both parties **extract gas** from offshore gas fields, which they own and operate independently from each other. Universal owns **55%** of the underground facility and Galaxy owns **45%**. They have agreed to share services and costs accordingly, with decisions regarding the storage facility requiring **unanimous agreement** of the parties. The underground facility is **pressurized** so that the **gas is pushed out** when extracted. When the gas **pressure is reduced** to a certain level, the **remaining gas is irrecoverable** and remains in the underground storage facility **until it is decommissioned**. **Local legislation** requires the decommissioning of the storage facility at the **end of its useful life**. Universal wishes to know how to treat the agreement with Galaxy including any obligation or possible obligation arising on the underground storage facility and the accounting for the irrecoverable gas.

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### Answer 34

The **classification** of a joint arrangement as a joint operation or a joint venture depends upon the **rights** and **obligations** of the parties to the arrangement (SLFRS 11 Joint Arrangements).

A joint arrangement occurs where two or more parties have joint control. The contractually agreed sharing of control of an arrangement exists only when decisions about the relevant activities require the unanimous consent of the parties sharing control. The structure and form of the arrangement determines the nature of the relationship.

However, regardless of the purpose, structure or form of the arrangement, the classification of joint arrangements depends upon the parties' rights and obligations arising from the arrangement.

A joint arrangement which is **not structured** through a **separate vehicle** is a joint operation. In such cases, the contractual arrangement establishes the parties' rights and obligations. A joint operator accounts for the assets, liabilities, revenues and expenses relating to its involvement in a joint operation in accordance with the relevant SLFRSs.

The arrangement with Galaxy is a joint operation as there is no separate vehicle involved and they have agreed to share services and costs with decisions regarding the platform requiring unanimous agreement of the parties. Universal should **recognize** its **share of the asset** as property, plant and equipment.

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### Answer 34

Under LKAS 16 Property, Plant and Equipment (PPE), the cost of an item of property, plant and equipment includes the initial estimate of the **costs of dismantling** and removing the item and restoring the site on which it is located.

LKAS 37 Provisions, Contingent Liabilities and Contingent Assets contains requirements on how to measure decommissioning, restoration and similar liabilities. Where the effect of the **time value of money** is **material**, the amount of a provision should be the **present value** of the expenditures expected to be required to settle the obligation. Thus, costs incurred by an entity in respect of obligations for dismantling, removing and restoring the site on which an item of property, plant and equipment is located are recognized and measured in accordance with LKAS 16 and LKAS 37.

Thus, **Universal** should **recognize 55%** of the cost of decommissioning the underground storage facility. However, because Universal is a joint operator, there is also a **contingent liability** for **45%** of the decommissioning costs and there is a possible obligation for the remainder of the costs depending on whether some uncertain future event occurs, that is Galaxy goes into **liquidation** and cannot fund the decommissioning costs. Therefore, Universal should also **disclose** a contingent liability relating to the Galaxy's share of the obligation to the extent that it is contingently liable for Galaxy's share.

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### Answer 34

LKAS 16 states that property, plant and equipment are tangible items which:

(a) are held for use in the production or supply of goods or services, for rental to others, or for administrative purposes; and

(b) are expected to be used during more than one period.

Thus, Universal should classify and account for its share of the **irrecoverable gas as PPE**. The irrecoverable gas is **necessary** for the storage facility to perform its function as a gas storage facility. It is therefore part of the storage facility and should be capitalized as a component of the storage facility asset. The irrecoverable gas should be **depreciated** to its **residual value** over the life of the storage facility.

However, if the gas is **recoverable in full** when the storage facility is decommissioned, then depreciation will be recorded against the irrecoverable gas component only if the estimated **residual value of the gas decreases below cost** during the life of the facility. When the storage facility is decommissioned and the cushion gas extracted and sold, the **sale of the irrecoverable gas** is accounted for as the **disposal of an item of PPE** in accordance with LKAS 16 and the gain or loss recognized in profit or loss. The **natural gas** in excess of the irrecoverable gas which is injected into the facility should be treated as **inventory** in accordance with LKAS 2 Inventories.

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## Accounting for Joint Ventures in Separate Financial Statements of Investors

Cost

Fair Value (SLFRS 09)

Equity Method

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