ASSURANCE AND ACCOUNTING

ASPE - IFRS: A Comparison

Joint Arrangements and Associates

In this publication we will examine the key differences between Accounting Standards for Private Enterprises (ASPE) and International Financial Reporting Standards (IFRS) related to joint arrangements and associates with a focus on:

- The classification and measurement of joint arrangements;
- Accounting for significantly influenced investments;
- The equity method;
- Impairment; and
- Contributions and transactions between an investor and investee;

References

ASPE	IFRS
• Section 3056 - *Interests in Joint Arrangements* • Section 3051 - *Investments* • Section 3856 - *Financial Instruments* • AcG-18 *Investment companies*	• IFRS 10 - *Consolidated Financial Statements* • IFRS 11 - *Joint Arrangements* • IAS 28 - *Investments in Associates and Joint Ventures* • IFRS 9 - *Financial Instruments*

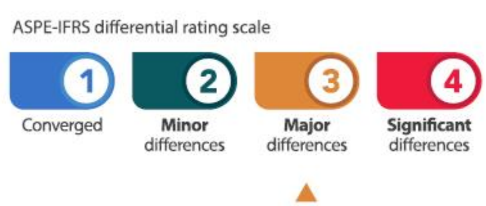
Overview of Major Differences

IFRS and ASPE have major differences in the accounting for joint arrangements and associates such as:

- ASPE has three joint arrangement classifications; whereas, IFRS only has two types of joint arrangements.

- ASPE provides an investor with an accounting policy choice to account for its interest in all jointly controlled enterprises using either the cost method, the equity method or by performing an analysis to determine whether it has the right to the individual assets and liabilities or a right to the net assets; whereas, IFRS requires the use of the equity method for joint venturers.

- ASPE allows for an accounting policy choice to account for significantly influenced investees using either the cost method or the equity method; whereas, IFRS requires the equity method be used to account for associates, other than in limited circumstances.



Definitions

Under both frameworks, a joint arrangement is defined as an arrangement that results from a contractual arrangement whereby two or more investors have joint control. However, IFRS provides more guidance on the typical terms included in a contractual arrangement.

ASPE	IFRS
The contractual arrangement that binds the investors may take different forms. For example, it may be evidenced by a contract between the investors or, in some cases, the arrangement may be incorporated into the articles or other by-laws of the joint arrangement. Whatever its form, the contractual arrangement is usually in writing and covers matters such as the purpose, activities, duration, policies and procedures of the joint arrangement, the allocation of ownership, the decision-making process, the capital contributions by the investors, and the sharing by the investors of the output, revenue, expenses or results of the joint arrangement. Activities conducted with no formal contractual arrangements that are jointly controlled in substance are considered joint arrangements.	A contractual arrangement can be enforceable by a written agreement, statutory mechanisms, by-laws or a separate vehicle. Appendix B of IFRS 11 identifies the terms that are generally included in contractual arrangements including: • The purpose, activity and duration of the joint arrangement; • How the members of the board of directors, or equivalent governing body, of the joint arrangement, are appointed; • The decision-making process: the matters requiring decisions from the parties, the voting rights of the parties and the required level of support for those matters (the decision-making process reflected in the contractual arrangement establishes joint control of the arrangement); • The capital or other contributions required of the parties; and • How the parties share assets, liabilities, revenues, expenses or profit or loss relating to the joint arrangement.

Joint Control

While both frameworks require joint control in a joint arrangement, it is defined differently. Under IFRS, joint control is based on the guidance in IFRS 10; whereas, under ASPE, all the guidance on joint control is contained in Section 3056. IFRS has a broader definition of joint control in that it also includes joint de-facto control.

ASPE	IFRS
Joint control of an economic activity is the contractually agreed sharing of the continuing power to determine its strategic operating, investing and financing policies. An investor that has joint control over a joint arrangement has the right and ability to obtain future economic benefits from the resources of the joint arrangement and is exposed to related risks. Future economic benefits normally include cash flows or other form of output generated by the joint arrangement, and related risks normally include exposure to losses of the joint arrangement or the direct exposure of the investor to loss.	Joint control is the contractually agreed sharing of control of an arrangement, which exists only when decisions about the relevant activities require the unanimous consent of the parties sharing control. An investor controls an investee if it has power over the investee, has exposure or right to variable returns from its involvement with the investee and has the ability to use its power over the investee to affect the amount of the investor's returns as defined in IFRS 10. (See our ASPE-IFRS: A Comparison Subsidiaries and Consolidation publication for more information on determining control).
Joint de-facto control is not addressed in Section 3056.	Joint de-facto control is based on the same de-facto control principles as IFRS 10. Joint de-facto control only

	exists if parties are contractually bound to vote together in relation to decisions on relevant activities. In assessing joint de-facto control, an entity may consider previous voting attendance but not previous voting results.
Section 3056 does not provide specific guidance on considering substantive or protective rights when determining joint control. Section 1591, *Subsidiaries*, provides general guidance on considering protective rights.	Substantive and protective rights, as defined in IFRS 10, also need to be considered in the assessment of joint control.

Classification of Joint Arrangements

Joint arrangements may take various forms and structures such as partnerships, co-tenancies, corporate or unincorporated enterprises or undivided interests. An entity must determine the type of joint arrangement in which it is involved as this impacts how the investment will be accounted for. The classification of a joint arrangement depends upon the rights and obligations of the parties to the arrangement.

ASPE	IFRS
There are three types of joint arrangements: jointly controlled operations, jointly controlled assets and jointly controlled enterprises.	There are two types of joint arrangements: joint ventures and joint operations.
Joint arrangements are classified based on their legal form, the terms of the contractual arrangement and other facts and circumstances.	While both frameworks identify the same factors to consider when assessing the terms of the contractual arrangement, IFRS provides more extensive guidance on classifying a joint arrangement than ASPE does.
A jointly controlled enterprise is an arrangement that involves the establishment of a corporation, partnership or other enterprise in which each investor has an interest. In a jointly controlled enterprise, an investor may have: • Rights to the individual assets and obligations for the individual liabilities of the jointly controlled enterprise; or • Rights to the net assets of a jointly controlled enterprise.	A joint arrangement that is not structured through a separate vehicle is a joint operation. A joint arrangement in which the assets and liabilities relating to the arrangement are held in a separate vehicle can be either a joint venture or a joint operation under IFRS depending on the rights and obligations of the parties. When the parties have structured a joint arrangement in a separate vehicle, the parties need to assess whether the legal form of the separate vehicle, the terms of the contractual arrangement and, when relevant, any other facts and circumstances give the investor: • Rights to the assets, and obligations for the liabilities, relating to the arrangement (i.e. the arrangement is a joint operation); or • Rights to the net assets of the arrangement (i.e. the arrangement is a joint venture).
A jointly controlled enterprise where the investor has rights to the net assets of the jointly controlled enterprise is similar to a joint venture under IFRS.	A joint venture is a joint arrangement whereby the parties that have joint control of the arrangement have rights to the net assets of the arrangement. Those parties are called joint venturers.

In a jointly controlled operation, the operations involve the use of the assets and other resources of the investors, rather than the establishment of a corporation, partnership or other enterprise, or a financial structure that is separate from the investors themselves. Each investor uses its own property, plant and equipment and carries its own inventories for the purposes of the joint arrangement activities. The assets remain under the ownership and control of each investor. Each investor also incurs its own expenses and liabilities and raises its own financing, which represents its own obligations. The joint arrangement activities may be carried out by the investor's employees alongside the investor's similar activities. The contractual arrangement usually provides a means by which the revenue from the sale of goods or services by the joint arrangement and any expenses incurred in common are shared among the investors.	A joint operation is a joint arrangement whereby the parties that have joint control of the arrangement have rights to the assets, and obligations for the liabilities, relating to the arrangement. Those parties are called joint operators. As noted above, a joint arrangement in which the assets and liabilities relating to the arrangement are held in a separate vehicle can be either a joint venture or a joint operation depending on the rights and obligations of the parties. A joint arrangement that is not structured through a separate vehicle is always a joint operation. There is no distinction between jointly controlled operations and jointly controlled assets under IFRS.
A jointly controlled asset arrangement involves the joint control, and often the joint ownership, by the investors of one or more assets contributed to, or acquired for the purpose of, the joint arrangement and dedicated to the purposes of the joint arrangement. Jointly controlled assets are used to obtain benefits for the investors. Each investor may take a share of the output from the assets and each bears an agreed share of the expenses incurred. Such a joint arrangement does not involve the establishment of a corporation, partnership or other enterprise, or a financial structure that is separate from the investors themselves.	

Financial Statements of Parties to a Joint Arrangement

The classification of a joint arrangement determines how the investor accounts for the joint arrangement. There are significant differences in the accounting for joint arrangements under ASPE and IFRS.

ASPE	IFRS
An investor in a jointly controlled operation in which the investor has joint control recognizes: • In its balance sheet, the assets that it controls and the liabilities that it incurs; and • In its income statement, its share of the revenue of the joint arrangement and its share of the expenses incurred by the joint arrangement.	A joint operator that has joint control and contractual rights to the assets and obligations of the joint operation, recognizes in relation to its interest in a joint operation: • Its assets, including its share of any assets held jointly; • Its liabilities, including its share of any liabilities incurred jointly; • Its revenue from the sale of its share of the output arising from the joint operation; and • Its expenses, including its share of any expenses incurred jointly An investor that does not have joint control but has contractual rights to the assets and obligations for the liabilities relating to the joint operation, must account for its contractual share of assets, liabilities, expenses and revenues in both its consolidated and individual
An investor in jointly controlled assets in which the investor has joint control recognizes: • In its balance sheet, its share of the jointly controlled assets and its share of any liabilities incurred jointly with the other investors in relation to the joint arrangement; and • In its income statement, any revenue from the sale or use of its share of the output of the joint arrangement, and its share of any expenses incurred by the joint arrangement.	

	financial statements and its separate financial statements.
An investor with an interest in a jointly controlled enterprise must make an accounting policy choice to: a) Account for all such interests using the equity method; b) Account for all such interests using the cost method; or c) Perform an analysis of each such interest and determine whether it represents a right to the net assets or to the individual assets and obligations for the individual liabilities relating to the joint arrangement and: i. Account for all interests in the net assets of a jointly controlled enterprise using either the cost or equity method; and ii. Account for all interests representing rights to the individual assets and obligations for the individual liabilities relating to a joint arrangement consistent with the accounting for jointly controlled operations and jointly controlled assets as described above. An investor must account for <u>all</u> interests in jointly controlled enterprises using the same method.	A joint venturer recognizes its interest in a joint venture as an investment and accounts for that investment using the equity method, unless the entity is exempted from applying the equity method as specified in IAS 28.(See Equity Method below) A party that participates in, but does not have joint control of, a joint venture must account for its interest in the arrangement in accordance with IFRS 9, unless it has significant influence over the joint venture, in which case it shall account for its interest in accordance with IAS 28.
There is no guidance in ASPE on the application of the business combinations guidance upon acquisition of an interest in a jointly operations or assets which meets the definition of a business. Section 1582, *Business Combinations,* scopes out joint arrangements.	When an entity acquires an interest in a joint operation in which the activity of the joint operation constitutes a business, as defined in IFRS 3, *Business Combinations,* the entity must apply, to the extent of its share, all of the principles on business combinations accounting in IFRS 3, and other IFRSs. This applies to the acquisition of both the initial interest and any additional interests in a joint operation in which the activity of the joint operation constitutes a business.

Significant Influence

Both frameworks presume that an investor that owns less than 20 per cent of an investee, does not have significant influence. Qualitative factors may also need to be considered to determine if an investor has significant influence. These factors include: representation on the board of directors, participation in policy-making processes, material intercompany transactions, interchange of managerial personnel or provision of technical information. The control of an investee by one entity does not preclude significant influence of the same investee by a different entity.

ASPE	IFRS
The scope of Section 3051 includes investments subject to significant influence and the measurement and disclosure of certain other non-financial instrument investments. It also applies to, an entity using the cost or equity method to account for its subsidiaries, and to an investor that uses the cost or equity method to account for its interest in a jointly controlled enterprise.	IAS 28 applies to all entities that are investors with joint control of a joint venture, or significant influence over, an investee. IFRS 9 applies to other financial instruments in an associate or joint venture to which the equity method is not applied. These include long-term interests that, in substance, form part of the entity's net investment in an associate or joint venture. An entity applies IFRS 9 to such long-term interests before it applies IAS 28. In

Section 3051 does not apply to subsidiaries or interests in joint arrangements, financial instruments and investments held by investment companies.	applying IFRS 9, the entity does not take account of any adjustments to the carrying amount of long-term interests that arise from applying IAS 28.
The term *investments subject to significant influence* is used to describe a relationship when an entity is able to exercise significant influence over the strategic operating, investing and financing policies of an investee without having control or joint control.	The term *associate* is used to describe a relationship when one entity has the power to participate in the financial and operating policy decisions of an investee, but does not have control or joint control over those policies.
The holding of 20 percent or more of the voting interest in an investee does not in itself confirm the ability to exercise significant influence.	If an entity holds, directly or indirectly, 20 per cent or more of the voting power of the investee, it is presumed that the entity has significant influence, unless it can be clearly demonstrated that this is not the case
ASPE is silent on what is included in potential voting interests in the determination of significant influence.	Any potential voting rights that are currently exercisable or convertible, including potential voting rights held by other entities and any contractual obligations are considered in assessing significant influence. Management intention and the financial ability to convert or exercise are not considered. However, equity accounting is based on actual interest only and not potential rights.

Accounting Methods

There is a significant difference in the accounting for investments between ASPE and IFRS. IFRS requires that investments be accounted for using the equity method with limited exceptions; whereas, ASPE provides an accounting policy choice to use the cost method or the equity method.

ASPE	IFRS
An investment subject to significant influence is accounted for using either the equity method or the cost method. An investor must make an accounting policy choice and account for all investments subject to significant influence using the same method. When an investee's equity securities are quoted in an active market, the investment cannot be accounted for using the cost method. Instead, it must be accounted for using the equity method or at its quoted amount with changes recorded in net income.	Associates are accounted for using the equity method with limited exceptions as described below. An entity need not apply the equity method to its investment in an associate or a joint venture if the entity is a parent company that is exempt from preparing consolidated financial statements, because it meets all of the following criteria: • The entity 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 entity not applying the equity method; • The entity'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); • The entity did not file, nor is it in the process of filing, its financial statements with a securities commission or other regulatory organization, for the purpose of issuing any class of instruments in a public market; and • The ultimate or any intermediate parent of the entity produces financial statements available for public use that comply with IFRSs, in which

	subsidiaries are consolidated or are measured at fair value through profit or loss in accordance with IFRS 10.
Under AcG-18, an investment company must measure all of its investments at fair value. This includes investments in joint arrangements, subsidiaries, or significantly-influenced investees. The only exceptions are: • A controlling interest in another investment company, when the parent investment company does not meet the requirements to account for the investment company subsidiary's investments at fair value (see below); and • An investment in an operating enterprise that provides services to the investment company (for example, an investment advisor).	When an investment in an associate or a joint venture is held by, or is held indirectly through, an entity that is a venture capital organization, or a mutual fund, unit trust or similar entities including investment-linked insurance funds, the investor may elect to measure its investments in those associates and joint ventures at fair value through profit or loss in accordance with IFRS 9.

Equity Method

Many of the procedures that are appropriate for the application of the equity method are similar to the consolidation procedures described in Section 1601, *Consolidated Financial Statements*, and IFRS 10, *Consolidated Financial Statements*.

ASPE	IFRS
As per Section 3051, the investment is initially recorded at cost and subsequently adjusted to include: • The investor’s pro rata share of post-acquisition earnings of the investee, computed using the consolidation method. The amount of the adjustment is included in determining the investor’s net income; • The investor’s investment account is increased / decreased to reflect the investor’s proportionate share of any capital transactions, discontinued operations, changes in accounting policies and corrections of errors relating to prior period financial statements applicable to post-acquisition periods; and • Profit distributions received / receivable from an investee reduce the carrying value of the investment.	As per IAS 28, The investment is initially recognized at cost and thereafter adjusted for the post-acquisition change in the investor’s share of the investee’s net assets. The investor’s share of the profit or loss of the investee is recognized in the investor’s profit or loss. Any distributions received from an investee reduce the carrying amount of the investment. Adjustments to the carrying amount may also arise from changes in the investee’s other comprehensive income (OCI) (i.e. revaluation of property, plant and equipment and foreign exchange translation differences). The investor’s share of those changes is recognized in OCI of the investor.
Depreciation and amortization of the investee assets are based on the assigned costs of such assets at the date(s) of acquisition. The portion of the difference between the investor's cost and the amount of its underlying equity in the net assets of the investee that is similar to goodwill is not amortized. No part of an impairment write-down of an investment accounted for by the equity method is presented in the income statement as a goodwill impairment loss.	An investment is accounted for using the equity method from the date on which it becomes an associate or a joint venture. On acquisition of the investment, any difference between the cost of the investment and the entity's share of the net fair value of the investee's identifiable assets and liabilities is accounted for as follows: • Goodwill relating to an associate or a joint venture is included in the carrying amount of the investment. Amortization of that goodwill is not permitted. • Any excess of the entity's share of the net fair value of the investee's identifiable assets and liabilities over the cost of the investment is included as income in the determination of the entity's share of

	the associate or joint venture's profit or loss in the period in which the investment is acquired.
An investor's share of losses in excess of the carrying amount of the investment are only recorded if: • The investor has guaranteed the obligations of the investee; • The investor is otherwise committed to provide further financial support to the investee; or • The investee seems assured of imminently returning to profitability. While ASPE is silent on the application of the losses in excess of the entity's investment, in practice, the same priority in liquidation concept set out in IFRS would be applied.	If an investor's share of losses of an investee exceeds its interest in the investee, the investor should discontinue recognizing its share of further losses. Losses recognized using the equity method in excess of the entity's investment in ordinary shares are applied to the other components of the entity's interest in an associate or a joint venture in the reverse order of their seniority (i.e. priority in liquidation). After the entity's interest is reduced to zero, additional losses are provided for, and a liability is recognized, only to the extent that the entity has incurred legal or constructive obligations or made payments on behalf of the associate or joint venture. If the associate or joint venture subsequently reports profits, the entity resumes recognising its share of those profits only after its share of the profits equals the share of losses not recognized.
When an investor ceases to account for an investment using the equity method, cost is deemed to be the carrying value of the investment at that time. Consideration is given to whether the carrying value requires adjustment to reflect an impairment in value. When an investor ceases to be able to exercise significant influence over an investee, the investor shall account for the investment as follows: • If the investor has obtained control of the investee, it accounts for its interest in accordance with Section 1591, *Subsidiaries*; • If the investor has obtained joint control of a jointly controlled enterprise, it accounts for its interest in accordance with Section 3056; • If the investor has a retained interest that represents rights to the individual assets and obligations for the individual liabilities of a joint arrangement, it accounts for its interests by applying the relevant standards for those assets and liabilities in accordance with Section 3056; or • If the investor has a retained interest in the investee that is a financial instrument, the investor accounts for the investment in accordance with, Section 3856.	When an entity discontinues the use of the equity method, the entity shall account for all amounts previously recognized in other comprehensive income in relation to that investment on the same basis as would have been required if the investee had directly disposed of the related assets or liabilities. If the retained interest in the former associate or joint venture is a financial asset, the entity shall measure the retained interest at fair value accordance with IFRS 9. The entity shall recognize in profit or loss any difference between: • The fair value of any retained interest and any proceeds from disposing of a part interest in the associate or joint venture; and • The carrying amount of the investment at the date the equity method was discontinued. If an investment in an associate becomes an investment in a joint venture or an investment in a joint venture becomes an investment in an associate, the entity continues to apply the equity method and does not remeasure the retained interest. A party that participates in, but does not have joint control of, a joint operation might obtain joint control of the joint operation in which the activity of the joint operation constitutes a business. In such cases, previously held interests in the joint operation are not remeasured. If an investment becomes a subsidiary, the entity follows the guidance in IFRS 3 and IFRS 10.
When calculating a gain or loss on the sale of an investment, the cost of the investment sold is calculated using the average carrying value. When an investor's interest in an investee accounted for using the equity method is diluted, any gains or losses	A dilution of interest is treated similarly under both frameworks. However, under IFRS, if ownership interest is reduced, but equity method remains, the entity reclassifies to profit or loss the gain or loss that had previously been recognized in OCI. There is no concept of OCI under ASPE.

arising from the dilution are recognized in income. This is consistent with the accounting for a gain or loss arising on the sale of a portion of an investment.	
An investor assesses whether there are any indications that an investment may be impaired at the end of each reporting period. Examples of indicators of impairment are identified in paragraph 24 of Section 3051. Under ASPE, testing an investment for impairment is a two-step process: 1. Determine whether there has been a significant adverse change in the expected timing or amount of future cash flows from the investment during the period. 2. If there is a change, the carrying amount of the investment is reduced to the higher of: • The present value of the cash flows expected to be generated by holding the investment, discounted using a current market rate of interest; and • The amount that could be realized by selling the asset at the balance sheet date. The guidance on reversals of impairment is converged with IFRS.	IFRS includes a similar list of impairment indicators to those outlined in Section 3051 in ASPE, however there are some differences for example under IFRS another indicator is a significant or prolonged decline in the fair value of an investment in an equity instrument below its cost. Goodwill that forms part of the carrying amount of an investment in an investee is not separately recognized and therefore not tested separately for impairment. Instead, the entire investment is tested as a single asset in accordance with IAS 36, *Impairment of Assets*. The impairment test and any reversals are done in accordance with IAS 36. (See our ASPE-IFRS: A Comparison Impairment of Non-Financial Assets publication)

Contributions and Transactions

Contributions and transactions between the investor and the joint arrangement in which it has joint control and also between the investor and the investee in a significantly influenced investment that is accounted for using the equity method are treated similarly under both frameworks, except that ASPE provides some specific guidance on related party transactions that does not exist under IFRS.

- **Sales or Contributions of Assets (downstream transactions):** When an investor **transfers assets** to a joint arrangement or significantly influenced investment (associate) and receives in exchange an interest in the joint arrangement or associate, or **sells assets** in the normal course of operations to such a joint arrangement or associate, any gain or loss that occurs is recognized in income at the time of the transfer or sale to the extent of the interests of the other non-related investors. When such a transaction provides evidence of a reduction in the net realizable value or a decline in the carrying amount of the relevant assets, the investor recognizes the decline by writing down the portion of the assets retained through its interest and recognizes the full amount of any loss in income immediately. Under ASPE, when the investors are related parties prior to the transfer of non-monetary assets, the guidance in Section 3840, *Related Party Transactions*. IFRS does not contain such guidance.

- **Purchases of Assets (upstream transactions):** When an investor **purchases assets** in the normal course of operations from a joint arrangement or significantly influenced investment (associate), the investor cannot recognize its share of the profit or loss of the joint arrangement / associate on the transaction until the assets are sold to a third party. When such a transaction provides evidence of a reduction in the net realizable value or a decline in the carrying amount of the relevant assets, the investor shall recognize this decline and recognize its share of the loss in income immediately.

Conclusion

In general, while the principles relating to accounting for joint arrangements and associates under ASPE and IFRS have some similarities, major differences can be identified when looking at the details of the standards.

If you require further guidance on accounting for joint arrangements and associates under IFRS or ASPE, please contact your local BDO Canada LLP office. If you are considering the adoption of a new standard, learn how our Accounting Advisory Services Team can help you with the transition.

To learn more about the differences between standards, view our ASPE-IFRS: A Comparison Series.