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including International Accounting Standards (IASs™) and Interpretations as at 31 March 2004

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International Accounting Standard 27

Consolidated and Separate Financial Statements

This version includes amendments resulting from new and amended IFRSs issued up to 31 March 2004. The section "Changes in this Edition" at the front of this volume provides the application dates of these new and amended IFRSs and also identifies those current IFRSs that are not included in this volume.

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International Accounting Standard 27 *Consolidated and Separate Financial Statements* (IAS 27) is set out in paragraphs 1-45 and the Appendix. All the paragraphs have equal authority but retain the IASC format of the Standard when it was adopted by the IASB. IAS 27 should be read in the context of the Basis for Conclusions, the *Preface to International Financial Reporting Standards* and the *Framework for the Preparation and Presentation of Financial Statements*. IAS 8 *Accounting Policies, Changes in Accounting Estimates and Errors* provides a basis for selecting and applying accounting policies in the absence of explicit guidance.

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Introduction

IN1. International Accounting Standard 27 *Consolidated and Separate Financial Statements* (IAS 27) replaces IAS 27 (revised 2000) *Consolidated Financial Statements and Accounting for Investments in Subsidiaries* and should be applied for annual periods beginning on or after 1 January 2005. Earlier application is encouraged. The Standard also replaces SIC-33 *Consolidation and Equity Method—Potential Voting Rights and Allocation of Ownership Interests*.

Reasons for Revising IAS 27

IN2. The International Accounting Standards Board developed this revised IAS 27 as part of its project on Improvements to International Accounting Standards. The project was undertaken in the light of queries and criticisms raised in relation to the Standards by securities regulators, professional accountants and other interested parties. The objectives of the project were to reduce or eliminate alternatives, redundancies and conflicts within the Standards, to deal with some convergence issues and to make other improvements.

IN3. For IAS 27 the Board's main objective was to reduce alternatives in accounting for subsidiaries in consolidated financial statements and in accounting for investments in the separate financial statements of a parent, venturer or investor. The Board did not reconsider the fundamental approach to consolidation of subsidiaries contained in IAS 27.

The Main Changes

IN4. The main changes from the previous version of IAS 27 are described below.

Scope

IN5. The Standard applies to accounting for investments in subsidiaries, jointly controlled entities and associates in the separate financial statements of a parent, a venturer or investor. Therefore, the title of the Standard was amended as shown in paragraph IN1.

Exemptions from Consolidating Investments in Subsidiaries

IN6. The Standard modifies the exemption from preparing consolidated financial statements. Paragraph 8 in the previous version of IAS 27 (now paragraph 10) was amended so that a parent need not present consolidated financial statements if:

(a) the parent is itself a wholly-owned subsidiary, or the parent 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 preparing consolidated financial statements;

(b) 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);

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(c) 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

(d) the ultimate or any intermediate parent of the parent produces consolidated financial statements available for public use that comply with International Financial Reporting Standards.

The Standard clarifies the requirements for a parent exempted from preparing consolidated financial statements when the parent elects, or is required by local regulations, to present separate financial statements (see paragraphs IN13 and IN14).

Temporary control

IN7. The Standard does not require consolidation of a subsidiary acquired when there is evidence that control is intended to be temporary. However, there must be evidence that the subsidiary is acquired with the intention to dispose of it within twelve months and that management is actively seeking a buyer. In addition, the words "in the near future" were replaced with the words "within twelve months". When a subsidiary previously excluded from consolidation is not disposed of within twelve months it must be consolidated as from the date of acquisition unless narrowly specified circumstances apply.

IN8. The Standard stipulates that the requirement to consolidate investments in subsidiaries applies to venture capital organisations, mutual funds, unit trusts and similar entities. This was added for clarification.

IN9. An entity is not permitted to exclude from consolidation an entity it continues to control simply because that entity is operating under severe long-term restrictions that significantly impair its ability to transfer funds to the parent. Control must be lost for exclusion to occur.

Consolidation Procedures

Potential voting rights

IN10. The Standard requires an entity to consider the existence and effect of potential voting rights currently exercisable or convertible when assessing whether it has the power to govern the financial and operating policies of another entity. This requirement was previously included in SIC-33, which has been superseded.

Accounting policies

IN11. The Standard requires an entity to use uniform accounting policies for reporting like transactions and other events in similar circumstances. The previous version of IAS 27 provided an exception to this requirement when it was "not practicable to use uniform accounting policies".

Minority interests

IN12. This Standard requires an entity to present minority interests in the consolidated balance sheet within equity, separately from the parent shareholders' equity. Though the previous version of IAS 27 precluded presentation of minority interests within liabilities, it did not require presentation within equity.

Separate Financial Statements

IN13. The Standard prescribes the accounting treatment for investments in subsidiaries, jointly controlled entities and associates when an entity elects, or is required by local regulations, to present separate financial statements. It requires these investments to be accounted for at cost or in accordance with IAS 39 *Financial Instruments: Recognition and Measurement*.

IN14. The Standard retains an alternative for accounting for these investments in an investor's separate financial statements. However, the Standard stipulates that when an entity accounts for investments in unconsolidated subsidiaries in accordance with IAS 39 in its consolidated financial statements, it must also do so in its separate financial statements.

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International Accounting Standard 27

Consolidated and Separate Financial Statements

Scope

*1. **This Standard shall be applied in the preparation and presentation of consolidated financial statements for a group of entities under the control of a parent.***

2. This Standard does not deal with methods of accounting for business combinations and their effects on consolidation, including goodwill arising on a business combination (see IFRS 3 *Business Combinations*).

*3. **This Standard shall also be applied in accounting for investments in subsidiaries, jointly controlled entities and associates when an entity elects, or is required by local regulations, to present separate financial statements.***

Definitions

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

Consolidated financial statements are the financial statements of a group presented as those of a single economic entity.

Control is the power to govern the financial and operating policies of an entity so as to obtain benefits from its activities.

The cost method is a method of accounting for an investment whereby the investment is recognised at cost. The investor recognises income from the investment only to the extent that the investor receives distributions from accumulated profits of the investee arising after the date of acquisition. Distributions received in excess of such profits are regarded as a recovery of investment and are recognised as a reduction of the cost of the investment.

A group is a parent and all its subsidiaries.

Minority interest is that portion of the profit or loss and net assets of a subsidiary attributable to equity interests that are not owned, directly or indirectly through subsidiaries, by the parent.

A parent is an entity that has one or more subsidiaries.

Separate financial statements are those presented by a parent, an investor in an associate or a venturer in a jointly controlled entity, in which the investments are accounted for on the basis of the direct equity interest rather than on the basis of the reported results and net assets of the investees.

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

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5. A parent or its subsidiary may be an investor in an associate or a venturer in a jointly controlled entity. In such cases, consolidated financial statements prepared and presented in accordance with this Standard are also prepared so as to comply with IAS 28 *Investments in Associates* and IAS 31 *Interests in Joint Ventures*.

6. For an entity described in paragraph 5, separate financial statements are those prepared and presented in addition to the financial statements referred to in paragraph 5. Separate financial statements need not be appended to, or accompany, those statements.

7. The financial statements of an entity that does not have a subsidiary, associate or venturer's interest in a jointly controlled entity are not separate financial statements.

8. A parent that is exempted in accordance with paragraph 10 from presenting consolidated financial statements may present separate financial statements as its only financial statements.

Presentation of Consolidated Financial Statements

9. A parent, other than a parent described in paragraph 10, shall present consolidated financial statements in which it consolidates its investments in subsidiaries in accordance with this Standard.

10. A parent need not present consolidated financial statements if and only if:

(a) the parent is itself 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;

(b) 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);

(c) 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

(d) the ultimate or any intermediate parent of the parent produces consolidated financial statements available for public use that comply with International Financial Reporting Standards.

11. A parent that elects in accordance with paragraph 10 not to present consolidated financial statements, and presents only separate financial statements, complies with paragraphs 37-42.

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Scope of Consolidated Financial Statements

12. Consolidated financial statements shall include all subsidiaries of the parent.*

13. Control is presumed to exist when the parent owns, directly or indirectly through subsidiaries, more than half of the voting power of an entity unless, in exceptional circumstances, it can be clearly demonstrated that such ownership does not constitute control. Control also exists when the parent owns half or less of the voting power of an entity when there is: †

    (a) power over more than half of the voting rights by virtue of an agreement with other investors;

    (b) power to govern the financial and operating policies of the entity under a statute or an agreement;

    (c) power to appoint or remove the majority of the members of the board of directors or equivalent governing body and control of the entity is by that board or body; or

    (d) power to cast the majority of votes at meetings of the board of directors or equivalent governing body and control of the entity is by that board or body.

14. An entity may own share warrants, share call options, debt or equity instruments that are convertible into ordinary shares, or other similar instruments that have the potential, if exercised or converted, to give the entity voting power or reduce another party's voting power over the financial and operating policies of another entity (potential voting rights). The existence and effect of potential voting rights that are currently exercisable or convertible, including potential voting rights held by another entity, are considered when assessing whether an entity has the power to govern the financial and operating policies of another entity. Potential voting rights are not currently exercisable or convertible when, for example, they cannot be exercised or converted until a future date or until the occurrence of a future event.

15. In assessing whether potential voting rights contribute to control, the 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 voting rights, except the intention of management and the financial ability to exercise or convert.

16. [Deleted]

17. [Deleted]

18. [Deleted]

19. A subsidiary is not excluded from consolidation simply because the investor is a venture capital organisation, mutual fund, unit trust or similar entity.

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* If on acquisition a subsidiary meets the criteria to be classified as held for sale in accordance with IFRS 5 *Non-current Assets Held for Sale and Discontinued Operations*, it shall be accounted for in accordance with that Standard.

† See also SIC-12 *Consolidation—Special Purpose Entities*.

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20. A subsidiary is not excluded from consolidation because its business activities are dissimilar from those of the other entities within the group. Relevant information is provided by consolidating such subsidiaries and disclosing additional information in the consolidated financial statements about the different business activities of subsidiaries. For example, the disclosures required by IAS 14 *Segment Reporting* help to explain the significance of different business activities within the group.

21. A parent loses control when it loses the power to govern the financial and operating policies of an investee so as to obtain benefit from its activities. The loss of control can occur with or without a change in absolute or relative ownership levels. It could occur, for example, when a subsidiary becomes subject to the control of a government, court, administrator or regulator. It could also occur as a result of a contractual agreement.

Consolidation Procedures

22. In preparing consolidated financial statements, an entity combines the financial statements of the parent and its subsidiaries line by line by adding together like items of assets, liabilities, equity, income and expenses. In order that the consolidated financial statements present financial information about the group as that of a single economic entity, the following steps are then taken:
    (a) the carrying amount of the parent's investment in each subsidiary and the parent's portion of equity of each subsidiary are eliminated (see IFRS 3, which describes the treatment of any resultant goodwill);
    (b) minority interests in the profit or loss of consolidated subsidiaries for the reporting period are identified; and
    (c) minority interests in the net assets of consolidated subsidiaries are identified separately from the parent shareholders' equity in them. Minority interests in the net assets consist of:
        (i) the amount of those minority interests at the date of the original combination calculated in accordance with IFRS 3; and
        (ii) the minority's share of changes in equity since the date of the combination.

23. When potential voting rights exist, the proportions of profit or loss and changes in equity allocated to the parent and minority interests are determined on the basis of present ownership interests and do not reflect the possible exercise or conversion of potential voting rights.

24. Intragroup balances, transactions, income and expenses shall be eliminated in full.

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25. Intragroup balances and transactions, including income, expenses and dividends, are eliminated in full. Profits and losses resulting from intragroup transactions that are recognised in assets, such as inventory and fixed assets, are eliminated in full. Intragroup losses may indicate an impairment that requires recognition in the consolidated financial statements. IAS 12 *Income Taxes* applies to temporary differences that arise from the elimination of profits and losses resulting from intragroup transactions.

26. The financial statements of the parent and its subsidiaries used in the preparation of the consolidated financial statements shall be prepared as of the same reporting date. When the reporting dates of the parent and a subsidiary are different, 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.

27. When, in accordance with paragraph 26, the financial statements of a subsidiary used in the preparation of consolidated financial statements are prepared as of a reporting date different from that of the parent, adjustments shall be made for the effects of significant transactions or events that occur between that date and the date of the parents financial statements. In any case, the difference between the reporting date of the subsidiary and that of the parent shall be no more than three months. The length of the reporting periods and any difference in the reporting dates shall be the same from period to period.

28. Consolidated financial statements shall be prepared using uniform accounting policies for like transactions and other events in similar circumstances.

29. If a member of the group uses accounting policies other than those adopted in the consolidated financial statements for like transactions and events in similar circumstances, appropriate adjustments are made to its financial statements in preparing the consolidated financial statements.

30. The income and expenses of a subsidiary are included in the consolidated financial statements from the acquisition date as defined in IFRS 3. The income and expenses of a subsidiary are included in the consolidated financial statements until the date on which the parent ceases to control the subsidiary. The difference between the proceeds from the disposal of the subsidiary and its carrying amount as of the date of disposal, including the cumulative amount of any exchange differences that relate to the subsidiary recognised in equity in accordance with IAS 21 *The Effects of Changes in Foreign Exchange Rates,* is recognised in the consolidated income statement as the gain or loss on the disposal of the subsidiary.

31. An investment in an entity shall be accounted for in accordance with IAS 39 **Financial Instruments: Recognition and Measurement** ***from the date that it ceases to be a subsidiary, provided that it does not become an associate as defined in IAS 28 or a jointly controlled entity as described in IAS 31.***

*32. **The carrying amount of the investment at the date that the entity ceases to be a subsidiary shall be regarded as the cost on initial measurement of a financial asset in accordance with IAS 39.***

*33. **Minority interests shall be presented in the consolidated balance sheet within equity, separately from the parent shareholders' equity. Minority interests in the profit or loss of the group shall also be separately disclosed.***

34. The profit or loss is attributed to the parent shareholders and minority interests. Because both are equity, the amount attributed to minority interests is not income or expense.

35. Losses applicable to the minority in a consolidated subsidiary may exceed the minority interest in the subsidiary's equity. The excess, and any further losses applicable to the minority, are allocated against the majority interest except to the extent that the minority has a binding obligation and is able to make an additional investment to cover the losses. If the subsidiary subsequently reports profits, such profits are allocated to the majority interest until the minority's share of losses previously absorbed by the majority has been recovered.

36. If a subsidiary has outstanding cumulative preference shares that are held by minority interests and classified as equity, the parent computes its share of profits or losses after adjusting for the dividends on such shares, whether or not dividends have been declared.

Accounting for Investments in Subsidiaries, Jointly Controlled Entities and Associates in Separate Financial Statements

*37. **When separate financial statements are prepared, investments in subsidiaries, jointly controlled entities and associates that are not classified as held for sale (or included in a disposal group that is classified as held for sale) in accordance with IFRS 5 shall be accounted for either:***

(a) at cost, or

(b) in accordance with IAS 39.

The same accounting shall be applied for each category of investments. Investments in subsidiaries, jointly controlled entities and associates that are classified as held for sale (or included in a disposal group that is classified as held for sale) in accordance with IFRS 5 shall be accounted for in accordance with that IFRS.

38. This Standard does not mandate which entities produce separate financial statements available for public use. Paragraphs 37 and 39-42 apply when an entity prepares separate financial statements that comply with International Financial Reporting Standards. The entity also produces consolidated financial statements available for public use as required by paragraph 9, unless the exemption provided in paragraph 10 is applicable.

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39. ***Investments in jointly controlled entities and associates that are accounted for in accordance with IAS 39 in the consolidated financial statements shall be accounted for in the same way in the investor's separate financial statements.***

Disclosure

40. ***The following disclosures shall be made in consolidated financial statements:***

    (a) [Deleted]

    (b) [Deleted]

    (c) ***the nature of the relationship between the parent and a subsidiary when the parent does not own, directly or indirectly through subsidiaries, more than half of the voting power;***

    (d) ***the reasons why the ownership, directly or indirectly through subsidiaries, of more than half of the voting or potential voting power of an investee does not constitute control;***

    (e) ***the reporting date of the financial statements of a subsidiary when such financial statements are used to prepare consolidated financial statements and are as of a reporting date or for a period that is different from that of the parent, and the reason for using a different reporting date or period; and***

    (f) ***the nature and extent of any significant restrictions (eg resulting from borrowing arrangements or regulatory requirements) on the ability of subsidiaries to transfer funds to the parent in the form of cash dividends or to repay loans or advances.***

41. ***When separate financial statements are prepared for a parent that, in accordance with paragraph 10, elects not to prepare consolidated financial statements, those separate financial statements shall disclose:***

    (a) ***the fact that the financial statements are separate financial statements; that the exemption from consolidation has been used; the name and country of incorporation or residence of the entity whose consolidated financial statements that comply with International Financial Reporting Standards have been produced for public use; and the address where those consolidated financial statements are obtainable;***

    (b) ***a list of significant investments in subsidiaries, jointly controlled entities and associates, including the name, country of incorporation or residence, proportion of ownership interest and, if different, proportion of voting power held; and***

    (c) ***a description of the method used to account for the investments listed under (b).***

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42. When a parent (other than a parent covered by paragraph 41), venturer with an interest in a jointly controlled entity or an investor in an associate prepares separate financial statements, those separate financial statements shall disclose:

- ***(a) the fact that the statements are separate financial statements and the reasons why those statements are prepared if not required by law;***
- ***(b) a list of significant investments in subsidiaries, jointly controlled entities and associates, including the name, country of incorporation or residence, proportion of ownership interest and, if different, proportion of voting power held; and***
- ***(c) a description of the method used to account for the investments listed under (b);***

and shall identify the financial statements prepared in accordance with paragraph 9 of this Standard, IAS 28 and IAS 31 to which they relate.

Effective Date

43. An entity shall apply this Standard for annual periods beginning on or after 1 January 2005. Earlier application is encouraged. If an entity applies this Standard for a period beginning before 1 January 2005, it shall disclose that fact.

Withdrawal of Other Pronouncements

44. This Standard supersedes IAS 27 *Consolidated Financial Statements and Accounting for Investments in Subsidiaries* (revised in 2000).

45. This Standard supersedes SIC-33 *Consolidation and Equity Method—Potential Voting Rights and Allocation of Ownership Interests.*

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Appendix

Amendments to Other Pronouncements

The amendments in this appendix shall be applied for annual periods beginning on or after 1 January 2005. If an entity applies this Standard for an earlier period, these amendments shall be applied for that earlier period.

* * * * *

The amendments contained in this appendix when this Standard was issued in 2003 have been incorporated into the relevant pronouncements published in this volume.

Approval of IAS 27 by the Board

International Accounting Standard 27 *Consolidated and Separate Financial Statements* was approved for issue by thirteen of the fourteen members of the International Accounting Standards Board. Mr Yamada dissented. His dissenting opinion is set out after the Basis for Conclusions.

Sir David Tweedie	Chairman
Thomas E Jones	Vice-Chairman
Mary E Barth	
Hans-Georg Bruns	
Anthony T Cope	
Robert P Garnett	
Gilbert Gélard	
James J Leisenring	
Warren J McGregor	
Patricia L O'Malley	
Harry K Schmid	
John T Smith	
Geoffrey Whittington	
Tatsumi Yamada	

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Basis for Conclusions

This Basis for Conclusions accompanies, but is not part of, IAS 27.

Introduction

BC1. This Basis for Conclusions summarises the International Accounting Standards Board's considerations in reaching its conclusions on revising IAS 27 *Consolidated Financial Statements and Accounting for Investments in Subsidiaries* in 2003. Individual Board members gave greater weight to some factors than to others.

BC2. In July 2001 the Board announced that, as part of its initial agenda of technical projects, it would undertake a project to improve a number of Standards, including IAS 27. The project was undertaken in the light of queries and criticisms raised in relation to the Standards by securities regulators, professional accountants and other interested parties. The objectives of the Improvements project were to reduce or eliminate alternatives, redundancies and conflicts within Standards, to deal with some convergence issues and to make other improvements. In May 2002 the Board published its proposals in an Exposure Draft of *Improvements to International Accounting Standards*, with a comment deadline of 16 September 2002. The Board received over 160 comment letters on the Exposure Draft.

BC3. Because the Board's intention was not to reconsider the fundamental approach to consolidation established in IAS 27, this Basis for Conclusions does not discuss requirements in IAS 27 that the Board has not reconsidered.

Presentation of Consolidated Financial Statements

Exemption from Preparing Consolidated Financial Statements

BC4. Paragraph 7 of the previous version of IAS 27 required consolidated financial statements to be presented. However, paragraph 8 permitted a parent that is a wholly-owned or virtually wholly-owned subsidiary not to prepare consolidated financial statements. The Board considered whether to withdraw or amend this exemption from the general requirement.

BC5. The Board decided to retain an exemption, so that entities in a group that are required by law to produce financial statements available for public use in accordance with International Financial Reporting Standards, in addition to consolidated financial statements, would not be unduly burdened.

BC6. The Board noted that in some circumstances users can find sufficient information for their purposes regarding a subsidiary from either its separate financial statements or consolidated financial statements. In addition, the users of financial statements of a subsidiary often have, or can get access to, more information.

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BC7. Having agreed to retain an exemption, the Board decided to modify the circumstances in which an entity would be exempt and considered the following criteria.

Unanimous agreement of the owners of the minority interests

BC8. The Exposure Draft proposed to extend the exemption to a parent that is not wholly-owned if the owners of the minority interest, including those not otherwise entitled to vote, unanimously agree.

BC9. Some respondents disagreed with the proposal for unanimous agreement of minority shareholders to be a condition for exemption, in particular because of the practical difficulties in obtaining responses from all of those shareholders. The Board decided that the exemption should be available to a parent that is not wholly-owned when the owners of the minority interests have been informed about, and do not object to, consolidated financial statements not being presented.

Exemption available only to non-public entities

BC10. The Board believes that the information needs of users of financial statements of entities whose debt or equity instruments are traded in a public market are best served when investments in subsidiaries, jointly controlled entities and associates are accounted for in accordance with IASs 27, 28 *Investments in Associates* and 31 *Interests in Joint Ventures*. The Board therefore decided that the exemption from preparing such consolidated financial statements should not be available to such entities or to entities in the process of issuing instruments in a public market.

BC11. The Board decided that a parent that meets the criteria for exemption from the requirement to prepare consolidated financial statements should, in its separate financial statements, account for those subsidiaries in the same way as other parents, venturers with interests in jointly controlled entities or investors in associates account for investments in their separate financial statements. The Board draws a distinction between accounting for such investments as equity investments and accounting for the economic entity that the parent controls. In relation to the former, the Board decided that each category of investment should be accounted for consistently.

BC12. The Board decided that the same approach to accounting for investments in separate financial statements should apply irrespective of the circumstances for which they are prepared. Thus, parents that present consolidated financial statements, and those that do not because they are exempted, should present the same form of separate financial statements.

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Scope of Consolidated Financial Statements

Scope Exclusions

BC13. Paragraph 13 of the previous version of IAS 27 required a subsidiary to be excluded from consolidation when control is intended to be temporary or when the subsidiary operates under severe long-term restrictions.

Temporary control

BC14. The Board considered whether to remove this scope exclusion and thereby converge with other standard-setters that had recently eliminated a similar exclusion. The Board decided to consider this issue as part of a comprehensive standard dealing with asset disposals. It decided to retain an exemption from consolidating a subsidiary when there is evidence that the subsidiary is acquired with the intention to dispose of it within twelve months and that management is actively seeking a buyer. The Board's Exposure Draft ED 4 *Disposal of Non-current Assets and Presentation of Discontinued Operations* proposes to measure and present assets held for sale in a consistent manner irrespective of whether they are held by an investor or in a subsidiary. Therefore, ED 4 proposes to eliminate the exemption from consolidation when control is intended to be temporary and contains a draft consequential amendment to IAS 27 to achieve this.*

Severe long-term restrictions impairing ability to transfer funds to the parent

BC15. The Board decided to remove the exclusion of a subsidiary from consolidation when there are severe long-term restrictions that impair a subsidiary's ability to transfer funds to the parent. It did so because such circumstances may not preclude control. The Board decided that a parent, when assessing its ability to control a subsidiary, should consider restrictions on the transfer of funds from the subsidiary to the parent. In themselves, such restrictions do not preclude control.

Venture capital organisations, private equity entities and similar organisations

BC16. The Exposure Draft of IAS 27 proposed to clarify that a subsidiary should not be excluded from consolidation simply because the entity is a venture capital organisation, mutual fund, unit trust or similar entity. Some respondents from the private equity industry disagreed with this proposed clarification. They argued that private equity entities should not be required to consolidate the investments they control in accordance with the requirements in IAS 27. They argued that they should measure those investments at fair value. Those respondents raised varying arguments—some based on whether control is exercised, some on the length of time that should be provided before consolidation is required, and some on whether consolidation was an appropriate basis for private equity entities or the type of investments they make.

* In March 2004, the Board issued IFRS 5 *Non-current Assets Held for Sale and Discontinued Operations*. IFRS 5 removes this scope exclusion and now eliminates the exemption from consolidation when control is intended to be temporary. See IFRS 5 Basis for Conclusions for further discussion.

BC17. Some respondents also noted that the Board decided to exclude venture capital organisations and similar entities from the scope of IASs 28 and 31 when investments in associates or jointly controlled entities are measured at fair value in accordance with IAS 39 *Financial Instruments: Recognition and Measurement*. In the view of these respondents, the Board was proposing that similar assets should be accounted for in dissimilar ways.

BC18. The Board did not accept these arguments. The Board noted that these issues are not specific to the private equity industry. It confirmed that a subsidiary should not be excluded from consolidation on the basis of the nature of the controlling entity. Consolidation is based on the parent's ability to control the investee, which captures both the power to control (ie the ability exists but it is not exercised) and actual control (ie the ability is exercised). Consolidation is triggered by control and should not be affected by whether management intends to hold an investment in an entity that it controls for the short term.

BC19. The Board noted that the exception from the consolidation principle in the previous version of IAS 27, when control of a subsidiary is intended to be temporary, might have been misread or interpreted loosely. Some respondents to the Exposure Draft had interpreted "near future" as covering a period of up to five years. The Board decided to remove these words and to restrict the exception to subsidiaries acquired and held exclusively for disposal within twelve months, providing that management is actively seeking a buyer.

BC20. The Board did not agree that it should differentiate between types of entity, or types of investment, when applying a control model of consolidation. It also did not agree that management intention should be a determinant of control. Even if it had wished to make such differentiations, the Board did not see how or why it would be meaningful to distinguish private equity investors from other types of entities.

BC21. The Board believes that the diversity of the investment portfolios of entities operating in the private equity sector is not different from the diversification of portfolios held by a conglomerate, which is an industrial group made up of entities that often have diverse and unrelated interests. The Board acknowledged that financial information about an entity's different types of products and services and its operations in different geographical areas—segment information—is relevant to assessing the risks and returns of a diversified or multinational entity and may not be determinable from the aggregated data presented in the consolidated balance sheet. The Board noted that IAS 14 *Segment Reporting* establishes principles for reporting segment information by entities whose equity or debt instruments are publicly traded, or any entity that discloses segment information voluntarily.

BC22. The Board concluded that for investments under the control of private equity entities, users' information needs are best served by financial statements in which those investments are consolidated, thus revealing the extent of the operations of the entities they control. The Board noted that a parent can either present information

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about the fair value of those investments in the notes to the consolidated financial statements or prepare separate financial statements in addition to its consolidated financial statements, presenting those investments at cost or at fair value. By contrast, the Board decided that information needs of users of financial statements would not be well served if those controlling investments were measured only at fair value. This would leave unreported the assets and liabilities of a controlled entity. It is conceivable that an investment in a large, highly geared subsidiary would have only a small fair value. Reporting that value alone would preclude a user from being able to assess the financial position, results and cash flows of the group.

Minority Interests

BC23. Minority interest is defined in IAS 27 and IFRS 3 *Business Combinations* as that part of the profit or loss and net assets of a subsidiary attributable to equity interests that are not owned, directly or indirectly through subsidiaries, by the parent. Paragraph 26 of the previous version of IAS 27 required minority interests to be presented in the consolidated balance sheet separately from liabilities and the parent shareholders' equity.

BC24. The Board decided to amend this requirement and to require minority interests to be presented in the consolidated balance sheet within equity, separately from the parent shareholders' equity. The Board agreed that a minority interest is not a liability of a group because it does not meet the definition of a liability in the *Framework for the Preparation and Presentation of Financial Statements*.

BC25. Paragraph 49(b) of the *Framework* states that a liability is a present obligation of the entity arising from past events, the settlement of which is expected to result in an outflow from the entity of resources embodying economic benefits. Paragraph 60 of the *Framework* further indicates that an essential characteristic of a liability is that the entity has a present obligation and that an obligation is a duty or responsibility to act or perform in a particular way. The Board noted that the existence of a minority interest in the net assets of a subsidiary does not give rise to a present obligation of the group, the settlement of which is expected to result in an outflow of economic benefits from the group.

BC26. Rather, the Board noted that a minority interest represents the residual interest in the net assets of those subsidiaries held by some of the shareholders of the subsidiaries within the group, and therefore meets the *Framework*'s definition of equity. Paragraph 49(c) of the *Framework* states that equity is the residual interest in the assets of the entity after deducting all its liabilities.

BC27. The Board acknowledged that this decision gives rise to questions about the recognition and measurement of minority interests but it concluded that the proposed presentation is consistent with current standards and the *Framework* and would provide better comparability than presentation in the consolidated balance sheet with either liabilities or parent shareholders' equity. It decided that the recognition and measurement questions should be addressed as part of its project on business combinations.

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Measurement of Investments in Subsidiaries, Jointly Controlled Entities and Associates in Separate Financial Statements

BC28. Paragraph 29 of the previous version of IAS 27 permitted investments in subsidiaries to be measured in any one of three ways in a parent's separate financial statements. These were cost, the equity method, or as available-for-sale financial assets in accordance with IAS 39. Paragraph 12 of the previous version of IAS 28 permitted the same choices for investments in associates in separate financial statements, and paragraph 38 of the previous version of IAS 31 mentioned that IAS 31 did not indicate a preference for any particular treatment for accounting for interests in jointly controlled entities in a venturer's separate financial statements. The Board decided to require use of cost or IAS 39 for all investments included in separate financial statements.

BC29. Although the equity method would provide users with some profit and loss information similar to that obtained from consolidation, the Board noted that such information is reflected in the investor's economic entity financial statements and does not need to be provided to the users of its separate financial statements. For separate statements, the focus is upon the performance of the assets as investments. The Board concluded that separate financial statements prepared using either the fair value method in accordance with IAS 39 or the cost method would be relevant. Using the fair value method in accordance with IAS 39 would provide a measure of the economic value of the investments. Using the cost method can result in relevant information, depending on the purpose of preparing the separate financial statements. For example, they may be needed only by particular parties to determine the dividend income from subsidiaries.

BC30. For investments in subsidiaries that are not consolidated in accordance with paragraph 16 of IAS 27 (ie because control is temporary), paragraph 30 of the previous version of IAS 27 permitted the same alternatives as were permitted in paragraph 29 of the previous version of IAS 27 for those that were consolidated—cost, the equity method, or as available-for-sale financial assets in accordance with IAS 39. The Board considered whether to eliminate one or more of these choices and decided that these subsidiaries should be accounted for consistently in both the consolidated and separate financial statements.

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Dissenting Opinion

DO1. Mr Yamada dissents from this Standard because he believes that the change in classification of minority interests in the consolidated balance sheet, that is to say, the requirement that it be shown as equity, should not be made as part of the Improvements project. He agrees that minority interests do not meet the definition of a liability under the *Framework for the Preparation and Presentation of Financial Statements,* as stated in paragraph BC25 of the Basis for Conclusions, and that the current requirement, for minority interests to be presented separately from liabilities and the parent shareholders' equity, is not desirable. However, he does not believe that this requirement should be altered at this stage. He believes that before making the change in classification, which will have a wide variety of impacts on current consolidation practices, various issues related to this change need to be considered comprehensively by the Board. These include consideration of the objectives of consolidated financial statements and the accounting procedures that should flow from those objectives. Even though the Board concluded as noted in paragraph BC27, he believes that the decision related to the classification of minority interests should not be made until such a comprehensive consideration of recognition and measurement is completed.

DO2. Traditionally, there are two views of the objectives of consolidated financial statements; they are implicit in the parent company view and the economic entity view. Mr Yamada believes that the objectives, that is to say, what information should be provided and to whom, should be considered by the Board before it makes its decision on the classification of minority interests in IAS 27. He is of the view that the Board is taking the economic entity view without giving enough consideration to this fundamental issue.

DO3. Step acquisitions are being discussed in the second phase of the Business Combinations project, which is not yet finalised at the time of finalising IAS 27 under the Improvements project. When the ownership interest of the parent increases, the Board has tentatively decided that the difference between the consideration paid by the parent to minority interests and the carrying value of the ownership interests acquired by the parent is recognised as part of equity, which is different from the current practice of recognising a change in the amount of goodwill. If the parent retains control of a subsidiary but its ownership interest decreases, the difference between the consideration received by the parent and the carrying value of the ownership interests transferred is also recognised as part of equity, which is different from the current practice of recognising a gain or a loss. Mr Yamada believes that the results of this discussion are predetermined by the decision related to the classification of minority interests as equity. The changes in accounting treatments are fundamental and he believes that the decision on which of the two views should govern the consolidated financial statements should be taken only after careful consideration of the ramifications. He believes that the amendment of IAS 27 relating to the classification of minority interests should not be made before completion of the second phase of the Business Combinations project.

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Implementation Guidance

Guidance on implementing IAS 27 *Consolidated and Separate Financial Statements*, IAS 28 *Investments in Associates* and IAS 31 *Interests in Joint Ventures*.

This guidance accompanies IAS 27, IAS 28 and IAS 31, but is not part of them.

Consideration of Potential Voting Rights

Introduction

IG1. Paragraphs 14, 15 and 23 of IAS 27 *Consolidated and Separate Financial Statements* and paragraphs 8 and 9 of IAS 28 *Investments in Associates* require an entity to consider the existence and effect of all potential voting rights that are currently exercisable or convertible. They also require all facts and circumstances that affect potential voting rights to be examined, except the intention of management and the financial ability to exercise or convert potential voting rights. Because the definition of joint control in paragraph 3 of IAS 31 *Interests in Joint Ventures* depends upon the definition of control, and because that Standard is linked to IAS 28 for application of the equity method, this guidance is also relevant to IAS 31.

Guidance

IG2. Paragraph 4 of IAS 27 defines control as the power to govern the financial and operating policies of an entity so as to obtain benefits from its activities. Paragraph 2 of IAS 28 defines significant influence as the power to participate in the financial and operating policy decisions of the investee but not to control those policies. Paragraph 3 of IAS 31 defines joint control as the contractually agreed sharing of control over an economic activity. In these contexts, power refers to the ability to do or effect something. Consequently, an entity has control, joint control or significant influence when it currently has the ability to exercise that power, regardless of whether control, joint control or significant influence is actively demonstrated or is passive in nature. Potential voting rights held by an entity that are currently exercisable or convertible provide this ability. The ability to exercise power does not exist when potential voting rights lack economic substance (eg the exercise price is set in a manner that precludes exercise or conversion in any feasible scenario). Consequently, potential voting rights are considered when, in substance, they provide the ability to exercise power.

IG3. Control and significant influence also arise in the circumstances described in paragraph 13 of IAS 27 and paragraphs 6 and 7 of IAS 28 respectively, which include consideration of the relative ownership of voting rights. IAS 31 depends on IAS 27 and IAS 28 and references to IAS 27 and IAS 28 from this point onwards should be read as being relevant to IAS 31. Nevertheless it should be borne in mind that joint control involves contractual sharing of control and this

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contractual aspect is likely to be the critical determinant. Potential voting rights such as share call options and convertible debt are capable of changing an entity's voting power over another entity—if the potential voting rights are exercised or converted, then the relative ownership of the ordinary shares carrying voting rights changes. Consequently, the existence of control (the definition of which permits only one entity to have control of another entity) and significant influence are determined only after assessing all the factors described in paragraph 13 of IAS 27 and paragraphs 6 and 7 of IAS 28 respectively, and considering the existence and effect of potential voting rights. In addition, the entity examines all facts and circumstances that affect potential voting rights except the intention of management and the financial ability to exercise or convert. The intention of management does not affect the existence of power and the financial ability of an entity to exercise or convert is difficult to assess.

IG4. An entity may initially conclude that it controls or significantly influences another entity after considering the potential voting rights that it can currently exercise or convert. However, the entity may not control or significantly influence the other entity when potential voting rights held by other parties are also currently exercisable or convertible. Consequently, an entity considers all potential voting rights held by it and by other parties that are currently exercisable or convertible when determining whether it controls or significantly influences another entity. For example, all share call options are considered, whether held by the entity or another party. Furthermore, the definition of control in paragraph 4 of IAS 27 permits only one entity to have control of another entity. Therefore, when two or more entities each hold significant voting rights, both actual and potential, the factors in paragraph 13 of IAS 27 are reassessed to determine which entity has control.

IG5. The proportion allocated to the parent and minority interests in preparing consolidated financial statements in accordance with IAS 27, and the proportion allocated to an investor that accounts for its investment using the equity method in accordance with IAS 28, are determined solely on the basis of present ownership interests. The proportion allocated is determined taking into account the eventual exercise of potential voting rights and other derivatives that, in substance, give access at present to the economic benefits associated with an ownership interest.

IG6. In some circumstances an entity has, in substance, a present ownership as a result of a transaction that gives it access to the economic benefits associated with an ownership interest. In such circumstances, the proportion allocated is determined taking into account the eventual exercise of those potential voting rights and other derivatives that give the entity access to the economic benefits at present.

IG7. IAS 39 *Financial Instruments: Recognition and Measurement* does not apply to interests in subsidiaries, associates and jointly controlled entities that are consolidated, accounted for using the equity method or proportionately consolidated in accordance with IAS 27, IAS 28 and IAS 31 respectively. When instruments containing potential voting rights in substance currently give access

to the economic benefits associated with an ownership interest, and the investment is accounted for in one of the above ways, the instruments are not subject to the requirements of IAS 39. In all other cases, instruments containing potential voting rights are accounted for in accordance with IAS 39.

Illustrative Examples

IG8. The five examples below each illustrate one aspect of a potential voting right. In applying IAS 27, IAS 28 or IAS 31, an entity considers all aspects. The existence of control, significant influence and joint control can be determined only after assessing the other factors described in IAS 27, IAS 28 and IAS 31. For the purpose of these examples, however, those other factors are presumed not to affect the determination, even though they may affect it when assessed.

Example 1: Options are out of the money

Entities A and B own 80 per cent and 20 per cent respectively of the ordinary shares that carry voting rights at a general meeting of shareholders of Entity C. Entity A sells one-half of its interest to Entity D and buys call options from Entity D that are exercisable at any time at a premium to the market price when issued, and if exercised would give Entity A its original 80 per cent ownership interest and voting rights.

Though the options are out of the money, they are currently exercisable and give Entity A the power to continue to set the operating and financial policies of Entity C, because Entity A could exercise its options now. The existence of the potential voting rights, as well as the other factors described in paragraph 13 of IAS 27, are considered and it is determined that Entity A controls Entity C.

Example 2: Possibility of exercise or conversion

Entities A, B and C own 40 per cent, 30 per cent and 30 per cent respectively of the ordinary shares that carry voting rights at a general meeting of shareholders of Entity D. Entity A also owns call options that are exercisable at any time at the fair value of the underlying shares and if exercised would give it an additional 20 per cent of the voting rights in Entity D and reduce Entity B's and Entity C's interests to 20 per cent each. If the options are exercised, Entity A will have control over more than one-half of the voting power. The existence of the potential voting rights, as well as the other factors described in paragraph 13 of IAS 27 and paragraphs 6 and 7 of IAS 28, are considered and it is determined that Entity A controls Entity D.

Example 3: Other rights that have the potential to increase an entity's voting power or reduce another entity's voting power

Entities A, B and C own 25 per cent, 35 per cent and 40 per cent respectively of the ordinary shares that carry voting rights at a general meeting of shareholders of Entity D. Entities B and C also have share warrants that are exercisable at any time at a fixed price and provide potential voting rights. Entity A has a call option to purchase these share warrants at any time for a nominal amount. If the call

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option is exercised, Entity A would have the potential to increase its ownership interest, and thereby its voting rights, in Entity D to 51 per cent (and dilute Entity B's interest to 23 per cent and Entity C's interest to 26 per cent).

Although the share warrants are not owned by Entity A, they are considered in assessing control because they are currently exercisable by Entities B and C. Normally, if an action (eg purchase or exercise of another right) is required before an entity has ownership of a potential voting right, the potential voting right is not regarded as held by the entity. However, the share warrants are, in substance, held by Entity A, because the terms of the call option are designed to ensure Entity A's position. The combination of the call option and share warrants gives Entity A the power to set the operating and financial policies of Entity D, because Entity A could currently exercise the option and share warrants. The other factors described in paragraph 13 of IAS 27 and paragraphs 6 and 7 of IAS 28 are also considered, and it is determined that Entity A, not Entity B or C, controls Entity D.

Example 4: Management intention

Entities A, B and C each own $33^{1}/_{3}$ per cent of the ordinary shares that carry voting rights at a general meeting of shareholders of Entity D. Entities A, B and C each have the right to appoint two directors to the board of Entity D. Entity A also owns call options that are exercisable at a fixed price at any time and if exercised would give it all the voting rights in Entity D. The management of Entity A does not intend to exercise the call options, even if Entities B and C do not vote in the same manner as Entity A. The existence of the potential voting rights, as well as the other factors described in paragraph 13 of IAS 27 and paragraphs 6 and 7 of IAS 28, are considered and it is determined that Entity A controls Entity D. The intention of Entity A's management does not influence the assessment.

Example 5: Financial ability

Entities A and B own 55 per cent and 45 per cent respectively of the ordinary shares that carry voting rights at a general meeting of shareholders of Entity C. Entity B also holds debt instruments that are convertible into ordinary shares of Entity C. The debt can be converted at a substantial price, in comparison with Entity B's net assets, at any time and if converted would require Entity B to borrow additional funds to make the payment. If the debt were to be converted, Entity B would hold 70 per cent of the voting rights and Entity A's interest would reduce to 30 per cent.

Although the debt instruments are convertible at a substantial price, they are currently convertible and the conversion feature gives Entity B the power to set the operating and financial policies of Entity C. The existence of the potential voting rights, as well as the other factors described in paragraph 13 of IAS 27, are considered and it is determined that Entity B, not Entity A, controls Entity C. The financial ability of Entity B to pay the conversion price does not influence the assessment.

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Table of Concordance

This table shows how the contents of the superseded version of IAS 27 and the current version of IAS 27 correspond. Paragraphs are treated as corresponding if they broadly address the same matter even though the guidance may differ.

The table also shows how the requirements of SIC Interpretation SIC-33 have been incorporated into the current version of IAS 27.

Superseded IAS 27 paragraph or Interpretation	Current IAS 27 paragraph
1	1
2	3
3	None
4	None
5	2
6	4
7	9
8	10, 41
9	None
10	None
11	12
12	13
13	None
14	20
15	22
16	None
17	24
18	25
19	26
20	27
21	28
22	29
23	30
24	31
25	32
26	33
27	35
28	36
29	37
30	39
31	3
32	40
33	43
SIC-33	14, 15
None	5-8
None	11
None	19
None	21
None	23
None	34
None	38
None	41, 42
None	44, 45