Accounting Standard (AS) 27
(issued 2002)

Financial Reporting of Interests in Joint Ventures

Contents

The following Accounting Standards Interpretations (ASIs) relate to AS 27:

- ASI 8 - Interpretation of the term 'Near Future'
- ASI 28 - Disclosure of parent's/venturer's shares in post-acquisition reserves of a subsidiary/jointly controlled entity.

The above Interpretations are published elsewhere in this Compendium.

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Financial Reporting of Interests in Joint Ventures

(This Accounting Standard includes paragraphs set in ***bold italic*** *type and plain type, which have equal authority. Paragraphs in bold italic type indicate the main principles. This Accounting Standard should be read in the context of its objective and the Preface to the Statements of Accounting Standards[1].)*

Accounting Standard (AS) 27, 'Financial Reporting of Interests in Joint Ventures', issued by the Council of the Institute of Chartered Accountants of India, comes into effect in respect of accounting periods commencing on or after 01.04.2002. In respect of separate financial statements of an enterprise, this Standard is mandatory in nature[2] from that date. In respect of consolidated financial statements of an enterprise, this Standard is mandatory in nature[2] where the enterprise prepares and presents the consolidated financial statements in respect of accounting periods commencing on or after 01.04.2002. Earlier application of the Accounting Standard is encouraged. The following is the text of the Accounting Standard.

Objective

The objective of this Statement is to set out principles and procedures for

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* A limited revision to this Standard has been made in 2004, pursuant to which paragraph 6 has been revised and paragraph 9 has been omitted (see footnotes 3 and 4).

[1] Attention is specifically drawn to paragraph 4.3 of the Preface, according to which Accounting Standards are intended to apply only to items which are material.

[2] Reference may be made to the section titled 'Announcements of the Council regarding status of various documents issued by the Institute of Chartered Accountants of India' appearing at the beginning of this Compendium for a detailed discussion on the implications of the mandatory status of an accounting standard.

accounting for interests in joint ventures and reporting of joint venture assets, liabilities, income and expenses in the financial statements of venturers and investors.

Scope

1. This Statement should be applied in accounting for interests in joint ventures and the reporting of joint venture assets, liabilities, income and expenses in the financial statements of venturers and investors, regardless of the structures or forms under which the joint venture activities take place.

2. The requirements relating to accounting for joint ventures in consolidated financial statements, contained in this Statement, are applicable only where consolidated financial statements are prepared and presented by the venturer.

Definitions

3. For the purpose of this Statement, the following terms are used with the meanings specified:

A joint venture is a contractual arrangement whereby two or more parties undertake an economic activity, which is subject to joint control.

Joint control is the contractually agreed sharing of control over an economic activity.

Control is the power to govern the financial and operating policies of an economic activity so as to obtain benefits from it.

A venturer is a party to a joint venture and has joint control over that joint venture.

An investor in a joint venture is a party to a joint venture and does not have joint control over that joint venture.

Proportionate consolidation is a method of accounting and reporting whereby a venturer's share of each of the assets, liabilities, income and expenses of a jointly controlled entity is reported as separate line items in the venturer's financial statements.

Forms of Joint Venture

4. Joint ventures take many different forms and structures. This Statement identifies three broad types - jointly controlled operations, jointly controlled assets and jointly controlled entities - which are commonly described as, and meet the definition of, joint ventures. The following characteristics are common to all joint ventures:

(a) two or more venturers are bound by a contractual arrangement; and

(b) the contractual arrangement establishes joint control.

Contractual Arrangement

5. The existence of a contractual arrangement distinguishes interests which involve joint control from investments in associates in which the investor has significant influence (see Accounting Standard (AS) 23, Accounting for Investments in Associates in Consolidated Financial Statements). Activities which have no contractual arrangement to establish joint control are not joint ventures for the purposes of this Statement.

6. In some exceptional cases, an enterprise by a contractual arrangement establishes joint control over an entity which is a subsidiary of that enterprise within the meaning of Accounting Standard (AS) 21, Consolidated Financial Statements. In such cases, the entity is consolidated under AS 21 by the said enterprise, and is not treated as a joint venture as per this Statement. The consolidation of such an entity does not necessarily preclude other venturer(s) treating such an entity as a joint venture.[3]

7. The contractual arrangement may be evidenced in a number of ways, for example by a contract between the venturers or minutes of discussions

[3] As a limited revision to AS 27, the Council of the Institute decided to revise this paragraph in 2004. The revision comes into effect in respect of accounting periods commencing on or after 1.4.2004 (see 'The Chartered Accountant', February 2004, pp. 820). The erstwhile paragraph was as under:
"6. In some exceptional cases, an enterprise by a contractual arrangement establishes joint control over an entity which is a subsidiary of that enterprise within the meaning of Accounting Standard (AS) 21, Consolidated Financial Statements. In such cases, the entity is not consolidated under AS 21, but is treated as a joint venture as per this Statement."

between the venturers. In some cases, the arrangement is incorporated in the articles or other by-laws of the joint venture. Whatever its form, the contractual arrangement is normally in writing and deals with such matters as:

(a) the activity, duration and reporting obligations of the joint venture;

(b) the appointment of the board of directors or equivalent governing body of the joint venture and the voting rights of the venturers;

(c) capital contributions by the venturers; and

(d) the sharing by the venturers of the output, income, expenses or results of the joint venture.

8. The contractual arrangement establishes joint control over the joint venture. Such an arrangement ensures that no single venturer is in a position to unilaterally control the activity. The arrangement identifies those decisions in areas essential to the goals of the joint venture which require the consent of all the venturers and those decisions which may require the consent of a specified majority of the venturers.

9. [4][***]

10. The contractual arrangement may identify one venturer as the operator or manager of the joint venture. The operator does not control the joint venture but acts within the financial and operating policies which have been agreed to by the venturers in accordance with the contractual arrangement and delegated to the operator.

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[4] As a limited revision to AS 27, the Council of the Institute decided to omit this paragraph in 2004. The revision came into effect in respect of accounting periods commencing on or after 1.4.2004 (see 'The Chartered Accountant', February 2004, pp. 820). The erstwhile paragraph was as under:

"9. The contractual arrangement will indicate whether or not an enterprise has joint control over the venture, along with the other venturers. In evaluating whether an enterprise has joint control over a venture, it would need to be considered whether the contractual arrangement provides protective rights or participating rights to the enterprise. Protective rights merely allow an enterprise to protect its interests in the venture in situations where its interests are likely to be adversely affected. The participating rights enable the enterprise to jointly control the financial and operating policies related to the venture's ordinary course of business. The existence of participating rights would evidence joint control."

Jointly Controlled Operations

11. The operation of some joint ventures involves the use of the assets and other resources of the venturers rather than the establishment of a corporation, partnership or other entity, or a financial structure that is separate from the venturers themselves. Each venturer uses its own fixed assets and carries its own inventories. It also incurs its own expenses and liabilities and raises its own finance, which represent its own obligations. The joint venture's activities may be carried out by the venturer's employees alongside the venturer's similar activities. The joint venture agreement usually provides means by which the revenue from the jointly controlled operations and any expenses incurred in common are shared among the venturers.

12. An example of a jointly controlled operation is when two or more venturers combine their operations, resources and expertise in order to manufacture, market and distribute, jointly, a particular product, such as an aircraft. Different parts of the manufacturing process are carried out by each of the venturers. Each venturer bears its own costs and takes a share of the revenue from the sale of the aircraft, such share being determined in accordance with the contractual arrangement.

13. In respect of its interests in jointly controlled operations, a venturer should recognise in its separate financial statements and consequently in its consolidated financial statements:

- ***(a) the assets that it controls and the liabilities that it incurs; and***
- ***(b) the expenses that it incurs and its share of the income that it earns from the joint venture.***

14. Because the assets, liabilities, income and expenses are already recognised in the separate financial statements of the venturer, and consequently in its consolidated financial statements, no adjustments or other consolidation procedures are required in respect of these items when the venturer presents consolidated financial statements.

15. Separate accounting records may not be required for the joint venture itself and financial statements may not be prepared for the joint venture. However, the venturers may prepare accounts for internal management reporting purposes so that they may assess the performance of the joint venture.

Jointly Controlled Assets

16. Some joint ventures involve the joint control, and often the joint ownership, by the venturers of one or more assets contributed to, or acquired for the purpose of, the joint venture and dedicated to the purposes of the joint venture. The assets are used to obtain economic benefits for the venturers. Each venturer may take a share of the output from the assets and each bears an agreed share of the expenses incurred.

17. These joint ventures do not involve the establishment of a corporation, partnership or other entity, or a financial structure that is separate from the venturers themselves. Each venturer has control over its share of future economic benefits through its share in the jointly controlled asset.

18. An example of a jointly controlled asset is an oil pipeline jointly controlled and operated by a number of oil production companies. Each venturer uses the pipeline to transport its own product in return for which it bears an agreed proportion of the expenses of operating the pipeline. Another example of a jointly controlled asset is when two enterprises jointly control a property, each taking a share of the rents received and bearing a share of the expenses.

19. In respect of its interest in jointly controlled assets, a venturer should recognise, in its separate financial statements, and consequently in its consolidated financial statements:

(a) its share of the jointly controlled assets, classified according to the nature of the assets;

(b) any liabilities which it has incurred;

(c) its share of any liabilities incurred jointly with the other venturers in relation to the joint venture;

(d) any income from the sale or use of its share of the output of the joint venture, together with its share of any expenses incurred by the joint venture; and

(e) any expenses which it has incurred in respect of its interest in the joint venture.

20. In respect of its interest in jointly controlled assets, each venturer includes in its accounting records and recognises in its separate financial statements and consequently in its consolidated financial statements:

(a) its share of the jointly controlled assets, classified according to the nature of the assets rather than as an investment, for example, a share of a jointly controlled oil pipeline is classified as a fixed asset;

(b) any liabilities which it has incurred, for example, those incurred in financing its share of the assets;

(c) its share of any liabilities incurred jointly with other venturers in relation to the joint venture;

(d) any income from the sale or use of its share of the output of the joint venture, together with its share of any expenses incurred by the joint venture; and

(e) any expenses which it has incurred in respect of its interest in the joint venture, for example, those related to financing the venturer's interest in the assets and selling its share of the output.

Because the assets, liabilities, income and expenses are already recognised in the separate financial statements of the venturer, and consequently in its consolidated financial statements, no adjustments or other consolidation procedures are required in respect of these items when the venturer presents consolidated financial statements.

21. The treatment of jointly controlled assets reflects the substance and economic reality and, usually, the legal form of the joint venture. Separate accounting records for the joint venture itself may be limited to those expenses incurred in common by the venturers and ultimately borne by the venturers according to their agreed shares. Financial statements may not be prepared for the joint venture, although the venturers may prepare accounts for internal management reporting purposes so that they may assess the performance of the joint venture.

Jointly Controlled Entities

22. A jointly controlled entity is a joint venture which involves the

establishment of a corporation, partnership or other entity in which each venturer has an interest. The entity operates in the same way as other enterprises, except that a contractual arrangement between the venturers establishes joint control over the economic activity of the entity.

23. A jointly controlled entity controls the assets of the joint venture, incurs liabilities and expenses and earns income. It may enter into contracts in its own name and raise finance for the purposes of the joint venture activity. Each venturer is entitled to a share of the results of the jointly controlled entity, although some jointly controlled entities also involve a sharing of the output of the joint venture.

24. An example of a jointly controlled entity is when two enterprises combine their activities in a particular line of business by transferring the relevant assets and liabilities into a jointly controlled entity. Another example is when an enterprise commences a business in a foreign country in conjunction with the government or other agency in that country, by establishing a separate entity which is jointly controlled by the enterprise and the government or agency.

25. Many jointly controlled entities are similar to those joint ventures referred to as jointly controlled operations or jointly controlled assets. For example, the venturers may transfer a jointly controlled asset, such as an oil pipeline, into a jointly controlled entity. Similarly, the venturers may contribute, into a jointly controlled entity, assets which will be operated jointly. Some jointly controlled operations also involve the establishment of a jointly controlled entity to deal with particular aspects of the activity, for example, the design, marketing, distribution or after-sales service of the product.

26. A jointly controlled entity maintains its own accounting records and prepares and presents financial statements in the same way as other enterprises in conformity with the requirements applicable to that jointly controlled entity.

Separate Financial Statements of a Venturer

27. In a venturer's separate financial statements, interest in a jointly controlled entity should be accounted for as an investment in accordance with Accounting Standard (AS) 13, Accounting for Investments.

28. Each venturer usually contributes cash or other resources to the jointly controlled entity. These contributions are included in the accounting records of the venturer and are recognised in its separate financial statements as an investment in the jointly controlled entity.

Consolidated Financial Statements of a Venturer

29. In its consolidated financial statements, a venturer should report its interest in a jointly controlled entity using proportionate consolidation except

(a) an interest in a jointly controlled entity which is acquired and held exclusively with a view to its subsequent disposal in the near future[5]; and

(b) an interest in a jointly controlled entity which operates under severe long-term restrictions that significantly impair its ability to transfer funds to the venturer.

Interest in such a jointly controlled entity should be accounted for as an investment in accordance with Accounting Standard (AS) 13, Accounting for Investments.

30. When reporting an interest in a jointly controlled entity in consolidated financial statements, it is essential that a venturer reflects the substance and economic reality of the arrangement, rather than the joint venture's particular structure or form. In a jointly controlled entity, a venturer has control over its share of future economic benefits through its share of the assets and liabilities of the venture. This substance and economic reality is reflected in the consolidated financial statements of the venturer when the venturer reports its interests in the assets, liabilities, income and expenses of the jointly controlled entity by using proportionate consolidation.

31. The application of proportionate consolidation means that the consolidated balance sheet of the venturer includes its share of the assets that it controls jointly and its share of the liabilities for which it is jointly responsible. The consolidated statement of profit and loss of the venturer includes its share of the income and expenses of the jointly controlled entity.

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[5] See also Accounting Standards Interpretation (ASI) 8, published elsewhere in this Compendium.

Many of the procedures appropriate for the application of proportionate consolidation are similar to the procedures for the consolidation of investments in subsidiaries, which are set out in Accounting Standard (AS) 21, Consolidated Financial Statements.

32. For the purpose of applying proportionate consolidation, the venturer uses the consolidated financial statements of the jointly controlled entity.

33. Under proportionate consolidation, the venturer includes separate line items for its share of the assets, liabilities, income and expenses of the jointly controlled entity in its consolidated financial statements. For example, it shows its share of the inventory of the jointly controlled entity separately as part of the inventory of the consolidated group; it shows its share of the fixed assets of the jointly controlled entity separately as part of the same items of the consolidated group.[6]

34. The financial statements of the jointly controlled entity used in applying proportionate consolidation are usually drawn up to the same date as the financial statements of the venturer. When the reporting dates are different, the jointly controlled entity often prepares, for applying proportionate consolidation, statements as at the same date as that of the venturer. When it is impracticable to do this, financial statements drawn up to different reporting dates may be used provided the difference in reporting dates is not more than six months. In such a case, adjustments are made for the effects of significant transactions or other events that occur between the date of financial statements of the jointly controlled entity and the date of the venturer's financial statements. The consistency principle requires that the length of the reporting periods, and any difference in the reporting dates, are consistent from period to period.

35. The venturer usually prepares consolidated financial statements using uniform accounting policies for the like transactions and events in similar circumstances. In case a jointly controlled entity uses accounting policies other than those adopted for the consolidated financial statements for like transactions and events in similar circumstances, appropriate adjustments are made to the financial statements of the jointly controlled entity when they are used by the venturer in applying proportionate consolidation. If it is

[6] See also Accounting Standards Interpretation (ASI) 28, published elsewhere in this Compendium.

not practicable to do so, that fact is disclosed together with the proportions of the items in the consolidated financial statements to which the different accounting policies have been applied.

36. While giving effect to proportionate consolidation, it is inappropriate to offset any assets or liabilities by the deduction of other liabilities or assets or any income or expenses by the deduction of other expenses or income, unless a legal right of set-off exists and the offsetting represents the expectation as to the realisation of the asset or the settlement of the liability.

37. Any excess of the cost to the venturer of its interest in a jointly controlled entity over its share of net assets of the jointly controlled entity, at the date on which interest in the jointly controlled entity is acquired, is recognised as goodwill, and separately disclosed in the consolidated financial statements. When the cost to the venturer of its interest in a jointly controlled entity is less than its share of the net assets of the jointly controlled entity, at the date on which interest in the jointly controlled entity is acquired, the difference is treated as a capital reserve in the consolidated financial statements. Where the carrying amount of the venturer's interest in a jointly controlled entity is different from its cost, the carrying amount is considered for the purpose of above computations.

38. The losses pertaining to one or more investors in a jointly controlled entity may exceed their interests in the equity[7] of the jointly controlled entity. Such excess, and any further losses applicable to such investors, are recognised by the venturers in the proportion of their shares in the venture, except to the extent that the investors have a binding obligation to, and are able to, make good the losses. If the jointly controlled entity subsequently reports profits, all such profits are allocated to venturers until the investors' share of losses previously absorbed by the venturers has been recovered.

39. A venturer should discontinue the use of proportionate consolidation from the date that:

(a) it ceases to have joint control over a jointly controlled entity but retains, either in whole or in part, its interest in the entity; or

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[7] Equity is the residual interest in the assets of an enterprise after deducting all its liabilities.

(b) the use of the proportionate consolidation is no longer appropriate because the jointly controlled entity operates under severe long-term restrictions that significantly impair its ability to transfer funds to the venturer.

40. From the date of discontinuing the use of the proportionate consolidation, interest in a jointly controlled entity should be accounted for:

(a) in accordance with Accounting Standard (AS) 21, Consolidated Financial Statements, if the venturer acquires unilateral control over the entity and becomes parent within the meaning of that Standard; and

(b) in all other cases, as an investment in accordance with Accounting Standard (AS) 13, Accounting for Investments, or in accordance with Accounting Standard (AS) 23, Accounting for Investments in Associates in Consolidated Financial Statements, as appropriate. For this purpose, cost of the investment should be determined as under:

(i) the venturer's share in the net assets of the jointly controlled entity as at the date of discontinuance of proportionate consolidation should be ascertained, and

(ii) the amount of net assets so ascertained should be adjusted with the carrying amount of the relevant goodwill/capital reserve (see paragraph 37) as at the date of discontinuance of proportionate consolidation.

Transactions between a Venturer and Joint Venture

41. When a venturer contributes or sells assets to a joint venture, recognition of any portion of a gain or loss from the transaction should reflect the substance of the transaction. While the assets are retained by the joint venture, and provided the venturer has transferred the significant risks and rewards of ownership, the venturer should recognise only that portion of the gain or loss which is attributable to the interests of the other venturers. The venturer should recognise the full amount of any loss when the contribution or sale provides evidence of a reduction in the net realisable value of current assets or an impairment loss.

42. When a venturer purchases assets from a joint venture, the venturer should not recognise its share of the profits of the joint venture from the transaction until it resells the assets to an independent party. A venturer should recognise its share of the losses resulting from these transactions in the same way as profits except that losses should be recognised immediately when they represent a reduction in the net realisable value of current assets or an impairment loss.

43. To assess whether a transaction between a venturer and a joint venture provides evidence of impairment of an asset, the venturer determines the recoverable amount of the asset as per Accounting Standard on Impairment of Assets[8]. In determining value in use, future cash flows from the asset are estimated based on continuing use of the asset and its ultimate disposal by the joint venture.

44. In case of transactions between a venturer and a joint venture in the form of a jointly controlled entity, the requirements of paragraphs 41 and 42 should be applied only in the preparation and presentation of consolidated financial statements and not in the preparation and presentation of separate financial statements of the venturer.

45. In the separate financial statements of the venturer, the full amount of gain or loss on the transactions taking place between the venturer and the jointly controlled entity is recognised. However, while preparing the consolidated financial statements, the venturer's share of the unrealised gain or loss is eliminated. Unrealised losses are not eliminated, if and to the extent they represent a reduction in the net realisable value of current assets or an impairment loss. The venturer, in effect, recognises, in consolidated financial statements, only that portion of gain or loss which is attributable to the interests of other venturers.[9]

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[8] Accounting Standard (AS) 28, 'Impairment of Assets', specifies the requirements relating to impairment of assets.

[9] An Announcement titled 'Elimination of unrealised profits and losses under AS 21, AS 23 and AS 27' has been issued in July 2004. As per the announcement, while applying 'proportionate consolidation method', elimination of unrealised profits and losses in respect of transactions entered into during accounting periods commencing on or before 31-3-2002, is encouraged, but not required on practical grounds.

Reporting Interests in Joint Ventures in the Financial Statements of an Investor

46. An investor in a joint venture, which does not have joint control, should report its interest in a joint venture in its consolidated financial statements in accordance with Accounting Standard (AS) 13, Accounting for Investments, Accounting Standard (AS) 21, Consolidated Financial Statements or Accounting Standard (AS) 23, Accounting for Investments in Associates in Consolidated Financial Statements, as appropriate.

47. In the separate financial statements of an investor, the interests in joint ventures should be accounted for in accordance with Accounting Standard (AS) 13, Accounting for Investments.

Operators of Joint Ventures

48. Operators or managers of a joint venture should account for any fees in accordance with Accounting Standard (AS) 9, Revenue Recognition.

49. One or more venturers may act as the operator or manager of a joint venture. Operators are usually paid a management fee for such duties. The fees are accounted for by the joint venture as an expense.

Disclosure

50. A venturer should disclose the information required by paragraphs 51, 52 and 53 in its separate financial statements as well as in consolidated financial statements.

51. A venturer should disclose the aggregate amount of the following contingent liabilities, unless the probability of loss is remote, separately from the amount of other contingent liabilities:

> ***(a) any contingent liabilities that the venturer has incurred in relation to its interests in joint ventures and its share in each of the contingent liabilities which have been incurred jointly with other venturers;***

(b) its share of the contingent liabilities of the joint ventures themselves for which it is contingently liable; and

(c) those contingent liabilities that arise because the venturer is contingently liable for the liabilities of the other venturers of a joint venture.

52. A venturer should disclose the aggregate amount of the following commitments in respect of its interests in joint ventures separately from other commitments:

(a) any capital commitments of the venturer in relation to its interests in joint ventures and its share in the capital commitments that have been incurred jointly with other venturers; and

(b) its share of the capital commitments of the joint ventures themselves.

53. A venturer should disclose a list of all joint ventures and description of interests in significant joint ventures. In respect of jointly controlled entities, the venturer should also disclose the proportion of ownership interest, name and country of incorporation or residence.

54. A venturer should disclose, in its separate financial statements, the aggregate amounts of each of the assets, liabilities, income and expenses related to its interests in the jointly controlled entities.