

**Statement of
Financial Accounting Standards
No. 31**

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Translated by

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Statement of Financial Accounting Standards No.31

Interests in Joint Ventures

I Introduction

- (1) This Statement establishes the accounting standards for venturers and investors in a joint venture. Joint venture in this Statement is the contractual arrangement whereby two or more parties undertake economic activities which are subject to joint control. Those activities that have no contractual arrangements are not within the scope of this Statement.

Certain interests in a joint venture held by the entities such as venture capital organizations, mutual funds, unit trusts and similar entities are excluded from the scope of this Statement if, at the time of initial recognition, such interests are designated as at fair value through profit or loss or classified as held for trading. Instead, such interests should follow the rules specified in the Statement of Financial Accounting Standards No. 34, *Financial Instruments: Recognition and Measurement*.

II Definitions

- (2) The definitions of the terms used in this Statement are as follows:
- (a) control: the power to govern and monitor the financial, operating and personnel policies of economic activities so as to obtain benefits from it.
 - (b) joint control: through contractual arrangement, two or more entities share the control of economic activities.

- (c) venturer: a party that participates in a joint venture and has joint control over that joint venture.
- (d) investor: a party that participates in a joint venture, but does not have joint control over that joint venture.

III Explanation

Types of joint ventures

- (3) Joint ventures have many different forms and structures. The joint ventures specified in this Statement have the following three types:
 - (a) jointly controlled operations;
 - (b) jointly controlled assets;
 - (c) joint controlled entities.

A joint venture usually has both of the following characteristics:

- (a) two or more venturers are bound by a contractual arrangement; and
- (b) the contractual arrangement establishes joint control.

Contractual arrangement

- (4) Contractual arrangements have many forms. For example, there are contracts or meeting minutes, joint venture articles or other forms of documents between venturers. Contractual arrangements are usually in writing and are related to the following contents:
 - (a) the economic activities, duration and reporting obligations of the joint venture;

- (b) the formation of the board of directors or equivalent governing body of the joint venture, and the voting right of each venturer;
 - (c) capital contribution of each venturer; and
 - (d) allocation of the output, revenue, expense or operating results of the joint venture to each venturer.
- (5) The contractual arrangement establishes joint control over the venturers, so that no single venturer can control the entire economic activity alone. Accordingly, the contractual arrangement specifies the items that require unanimous consent (especially the decisions that are related to the joint venture objectives), and the items that must have majority consent of the venturers.
 - (6) Contractual arrangement may designate one of the venturers as the manager of the joint venture. The manager, in substance, does not have control over the joint venture activities, but is only authorized to execute the financial, operating, and personnel policies that are approved by the venturers according to the contractual arrangement.

Jointly controlled operations

- (7) The jointly controlled operations involve the use of the venturers' assets and other resources rather than establishing a corporation, partnership or any other form of entity. Each venturer uses its own properties, plant and equipment and holds its own inventory. It also assumes its own expenses and liabilities, and arranges its own financing. Jointly controlled operations may concur with the venturer's own operations. The contractual arrangement usually specifies the allocation method for product revenues and common costs of joint production.
- (8) A jointly controlled operation may be when two or more venturers combine their operations, resources and expertise in order to manufacture, market and distribute jointly a particular product. For

example, aircraft manufacturing in accordance with the contractual arrangement, whereby each venturer is responsible for the production of specific parts of the aircraft, bears its own production costs, and shares the revenue from the sale of the aircraft.

- (9) A joint venture of jointly controlled operation need not have independent accounting records and financial statements. However, a venturer may prepare its own management reports for the purpose of performance evaluation.

Jointly controlled assets

- (10) A venturer of jointly controlled assets contributes or acquires one or more assets as its investment in the agreed-upon business operation. The venturers jointly control or own such assets to obtain economic benefits. Each venturer shares in the output and the expenses according to the contractual arrangement.
- (11) These joint ventures do not involve the establishment of a corporation, partnership, or any other form of entity that is separate from the venturers themselves. Each venturer usually exercises its right according to its share of jointly owned assets.
- (12) The exploration of oil, natural gas or minerals may be carried out in the form of jointly controlled assets. For example, several oil companies may jointly control and use the same oil pipeline. Each venturer uses the oil pipeline to transport the oil that it has exploited and, in return, bears an agreed proportion of the pipeline expenses. Another example of jointly controlled assets is when two enterprises jointly control an asset, each taking a share of the rental income and bearing a share of the rental expenses.
- (13) The purpose of the accounting for jointly controlled assets is to reflect the economic substance of the joint venture. Therefore, the joint venture accounting records for jointly controlled assets may be limited to the regular expenses that are commonly shared by the venturers. The joint venture need not have independent financial statements. However, a venturer may prepare its own management

reports for the purpose of performance evaluation.

Jointly controlled entities

- (14) A jointly controlled entity is a joint venture whereby the venturers collectively establish a corporation, partnership or any other form of entity. The difference between a jointly controlled entity and an ordinary enterprise is that the venturers use a contractual arrangement to establish joint control over the entity's economic activity.
- (15) A jointly controlled entity controls the assets of the joint venture, assumes liabilities and expenses, and earns profits. The jointly controlled entity can use its own name to sign contracts and raise funds. In general, the venturers of a jointly controlled entity share the operating results of the joint venture, but may also share its output.
- (16) The following are common examples of jointly controlled entities:
- (a) Two enterprises transfer related assets and liabilities to a jointly controlled entity for a certain kind of business.
 - (b) An enterprise cooperates with the government or other agency in a foreign country to engage in a certain kind of business, by establishing a separate entity which is jointly controlled by both parties.
- (17) Jointly controlled entities are often similar in substance to jointly controlled operations and jointly controlled assets. For example, a jointly controlled operation sometimes set up a jointly controlled entity to engage in a particular kind of economic activity, such as product design, marketing, or after-sales service, etc. In such circumstances, the jointly controlled entity is similar to the jointly controlled operation. Moreover, the venturers may, for tax or other reasons, transfer jointly controlled assets to a jointly controlled entity for joint control and use. Or the venturers may also provide their own assets to a jointly controlled entity for its operating use. In such

circumstances, the jointly controlled entities are similar to the jointly controlled assets.

- (18) A jointly controlled entity must have independent accounting records, and its accounting treatment must follow Generally Accepted Accounting Principles.

Equity method

- (19) As a venturer may, in substance, only have significant influence rather than control over the jointly controlled entity. As such, the equity method is used to account for the venturer's interest in the jointly controlled entity, and the venturer need not prepare consolidated financial statements using the proportionate consolidation method.

Proportionate consolidation method

- (20) A venturer may consider that consolidation financial statements better reflect the economic substance of its interest in the jointly controlled entity; thus, the venturer may use the proportionate consolidation method to prepare consolidated financial statements.

IV Accounting standards

Jointly controlled operations

- (21) To present its interests in jointly controlled operations, a venturer should recognize the following items in its separate financial statements:
- (a) the assets that it controls and the liabilities that it bears; and
 - (b) the revenue and expenses that it shares.

Jointly controlled assets

- (22) To present its interests in jointly controlled assets, a venturer should

recognize the following items in its separate financial statements:

- (a) its share of jointly controlled assets, classified according to the nature of the assets rather than as *investments*. For example, oil pipeline should be classified under *fixed assets*;
- (b) the liabilities which it has separately incurred. For example, the liabilities incurred to purchase jointly controlled assets;
- (c) its share of the joint liabilities that the joint venture incurred;
- (d) the expenses which is has separately incurred. For example, the expenses incurred related to the financing of jointly controlled assets purchased or to the sale of joint venture products; and
- (e) its share of common revenue and expenses incurred by the joint venture.

Jointly controlled entities

Equity method

- (23) The cash or other assets that a venturer contributes into a jointly controlled entity should be recognized as *Investments*. Except for the rules stated in Paragraph 27, a venturer should use the equity method to account for such investments and follow the principles outlined in the Statements of Financial Accounting Standards No. 5, *Long-Term Investments in Equity Securities*.

Proportionate consolidation method

- (24) A venturer does not have to prepare consolidated financial statements to account for its interests in a jointly controlled entity. If the venturer elects to prepare consolidated financial statements, the proportionate consolidation method should be applied. But when the jointly controlled entity becomes the subsidiary of the venturer, the venturer should follow the principles outlined in the Statements of Financial Accounting Standards No. 5, *Long-Term Investments in*

Equity Securities and the Statements of Financial Accounting Standards No. 7, *Consolidated Financial Statements*.

- (25) When a venturer uses the proportionate consolidation method to prepare financial statements, it can either group by accounts or present separately by category. The principles outlined in the Statements of Financial Accounting Standards No. 7, *Consolidated Financial Statements* can be applied.

For those who group by accounts, the venturers' proportionate share of assets, liabilities, revenue and expenses accounts of jointly controlled entities should be combined into similar accounts in the venturers' financial statements. For example, a venturer should combine its proportionate share of inventory and machinery equipment in a jointly controlled entity into its own inventory and machinery equipment accounts.

For those who present separately by category, the venturers' proportionate share of assets, liabilities, revenue and expenses accounts of jointly controlled entities should first be listed separately in the venturers' consolidated financial statements, and then combined with similar accounts. For example, a venturer should present its proportionate share of current assets and fixed assets in a jointly controlled entity as separate items in the current assets and fixed assets sections of the consolidated financial statements, and then these items should be added to other similar accounts.

- (26) When a venturer loses its joint control over a jointly controlled entity, use of the proportionate consolidation method should be discontinued. For example, a venturer transfers its interests in a jointly controlled entity to other parties or the environment or the law imposes restrictions on a jointly controlled entity so that it can no longer achieve its purposes, then the venturer should discontinue the use of the proportionate consolidation method.

Exceptions

- (27) A venturer with an interest in a jointly controlled entity is exempted

from applying the equity method or the proportionate consolidation method when the interest is held primarily for sale or intended for sale. Moreover, the interest in a jointly controlled entity must be available for immediate sale in its present condition only to the terms that are usual and customary for such sale. And the sale is highly probable for the venturer to sell the interest in a jointly controlled entity.

The afore-mentioned "highly probable sale" should be referred to the criteria for highly probable sale in the Statement of Financial Accounting Standards No. 7: *Consolidated Financial Statements*. Such interest should be measured at the lower of carrying amount and net fair value. The loss or reversed gain resulting from measurement should be recognized in current profit or loss. If the interest is not disposed within one year after it was acquired, the interest should apply the equity method or the proportionate consolidation method from the date of acquisition. The previous financial statements should be restated if they had not applied the equity method or the proportionate consolidation method, unless there are events or circumstances that are beyond the control of the venturer so that the sale transaction is delayed for more than one year, and there are sufficient evidences that the venturer still maintains its commitment to sell.

Accounting for investors in a joint venture

- (28) If a venturer has significant influence over the joint venture, the equity method should be applied; otherwise, it should follow the rules specified in the SFAS No. 34: *Financial Instruments: Recognition and Measurement*.

Operators of joint ventures

- (29) A venturer may be responsible for the operation and management of the joint venture, and the resulting compensation received by the venturer should be accounted for as revenue. The compensation paid by the joint venture should be accounted for as an expense.

Disclosure

- (30) A venturer of jointly controlled operations or jointly controlled assets should disclose in details its interests recognized in accordance with the rules stated in paragraph 21 and 22.

A venturer of jointly controlled entities should disclose in details its proportionate interests in jointly controlled entities, and its share of current assets, noncurrent assets, current liabilities, long-term liabilities, revenue and expenses of all jointly controlled entities.

- (31) To account for contingencies, a venturer should follow the principles outlined in the Statements of Financial Accounting Standards No. 9, *Contingencies and Subsequent Events*. The following contingencies, if material, should be disclosed separately from other contingencies:

- (a) any contingencies that the venturer has incurred in relation to its interests in a joint venture;
- (b) its share of the contingencies that are incurred jointly by the venturer and other venturers;
- (c) its share of the contingencies that are incurred by the joint venture; and
- (d) any contingencies that the venturer incurs resulting from other venturers' obligations.

- (32) A venturer should disclose the following commitments separately from other commitments:

- (a) any capital commitments of the venturer in relation to its interests in the joint venture;
- (b) its share in the capital commitments that have been incurred jointly with other venturers;
- (c) its share of the capital commitments that the joint venture has made.

V Notes

- (33) Investment in a joint venture that was prior to the Statement's effective date and did not follow the principles set out in this Statement need not be restated.
- (34) This Statement was issued on September 7, 2000. The first revision of this Statement was on September 22, 2005.

The provisions of the first revision shall be effective for financial statements for the fiscal year beginning on or after January 1, 2006. Earlier adoption is not permitted.

The provisions of this Statement need not be applied to immaterial items.
