

Amendments to HKFRS 11 - Accounting for Acquisitions of Interests in Joint Operations

Introduction

HKFRS 11 “Joint Arrangements” does not provide any guidance on the accounting of the joint operators for acquisitions of interests in joint operations in which the activities of the joint operations constitute businesses (as defined in HKFRS 3 “Business Combinations”). The following diversities in accounting practice are noted:

HKFRS 3 approach

The acquisitions were accounted for using the guidance in HKFRS 3. Identifiable assets and liabilities were initially measured at fair value and the residual of the acquisition costs was recognised as goodwill. Transaction costs were expensed. Deferred taxes were recognised on initial recognition of assets and liabilities.

Cost approach

The acquisition costs were allocated to the individual identifiable assets on the basis of their relative fair values. Transaction costs were capitalised. Deferred taxes were not recognised.

Hybrid approach

Identifiable assets and liabilities were initially measured at fair value and the residual of the acquisition costs was recognised as goodwill. However, transaction costs were capitalised. Contingent liabilities and deferred taxes were not recognised.

In order to eliminate the above diversities, HKFRS 11 is amended to provide guidance on the accounting for acquisitions of interests in joint operations in which the activities of the joint operations constitute businesses.

We understand that the original objective of the amendments is to provide guidance on the accounting of the joint operators only, for acquisitions of interests in joint operations in which the activities of the joint operations constitute businesses. However, the term used in the amendments for the acquiring party is mainly ‘an entity’ instead of ‘a joint operator’. In addition, paragraph 23 of HKFRS 11 requires that a party that participates in, but does not have joint control of, a joint operation shall also account for its interest in the arrangement in accordance with paragraphs 20 to 22 of HKFRS 11 if that party has rights to the assets, and obligations for the liabilities, relating to the joint operation. Paragraphs 20 to 22 of HKFRS 11 are the accounting requirements for joint operators and now also include the requirements of the amendments (paragraph 21A and further expanded by paragraphs B33A to B33D). As a result, we are of the view that a party to the joint operation but does not have joint control will also need to follow the requirements of the amendments if that party has rights to the assets, and obligations for the liabilities, relating to the joint operation.

Scope

The amendments apply to the acquisitions of both the initial interest and additional interests in a joint operation in which the activity of the joint operation constitutes a business.

The amendments also apply to the formation of a joint operation when an existing business is contributed to the joint operation on its formation by one of the parties that participate in the joint operation. The contributing party can be a joint operator or a party to the joint operation but does not have joint control.

The amendments do not apply to the formation of a joint operation if all of the parties that participate in the joint operation only contribute assets or groups of assets that do not constitute businesses to the joint operation on its formation i.e. no existing business is contributed to the joint operation on its formation. This also includes the case when the formation of the joint operation coincides with the formation of the business.

The amendments do not apply on the acquisition of an interest in a joint operation when the parties sharing joint control, including the entity acquiring the interest in the joint operation, are under the common control of the same ultimate controlling party or parties both before and after the acquisition, and that control is not transitory.

Effective Date and Transitional Provision

An entity shall apply the amendments prospectively for acquisitions of interests in joint operations in which the activities of the joint operations constitute businesses, for those acquisitions occurring from the beginning of the first annual period beginning on or after 1 January 2016. Amounts recognised for acquisitions of interests in joint operations occurring in prior periods shall not be adjusted.

Earlier application is permitted. If an entity applies the amendments in an earlier period it shall disclose that fact.



Summary of Amendments

When a joint operator acquires an interest in a joint operation in which the activity of the joint operation constitutes a business, it shall apply, to the extent of its share of the assets and liabilities of the joint operation, all of the principles on business combinations accounting in HKFRS 3 and other HKFRSs, that do not conflict with the guidance in HKFRS 11. Such principles include but are not limited to:

- (a) measuring identifiable assets and liabilities at fair value;
- (b) recognising acquisition-related costs as expenses except for the costs to issue debt or equity securities;
- (c) recognising deferred tax assets and deferred tax liabilities;
- (d) recognising the excess of the consideration transferred over the net of the acquisition-date fair value of the identifiable assets and liabilities as goodwill; and
- (e) testing for impairment a cash-generating unit to which goodwill has been allocated at least annually.



When a joint operator increases its interest in a joint operation in which the activity of the joint operation constitutes a business, by acquiring an additional interest in the joint operation, previously held interests in the joint operation are not remeasured if the joint operator retains joint control.

The joint operator acquiring an interest in a joint operation in which the activity of the joint operation constitutes a business shall disclose the information required by HKFRSs in relation to business combinations.

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