HMRC - OT02115 - Joint Venture Accounting - UKGAAP

The accounting standard applicable to Joint ventures in UKGAAP is FRS 9, Associates and Joint Ventures. The SORP contains recommendations specific to the oil and gas sector. Below is a summary of the definitions of an associate and joint venture given in FRS 9.

An associate is defined as an entity (other than a subsidiary) in which another entity (the investor) has a participating interest and over whose operating and financial policies the investor exercises a significant influence.

The participating interest must be held on a long-term basis where benefits are expected to accrue from the exercise of significant influence over operating and financial policies.

FRS9 contains guidance for joint arrangements that are not entities (JANE’s).

A JANE is a contractual arrangement under which the participants engage in joint activities that do not create an entity because it would not be carrying on a trade or business of its own. A contractual arrangement where all significant matters of operating and financial policy are predetermined does not create an entity because the policies are those of its participants not of a separate entity.

A joint venture is defined as “an entity in which the reporting entity holds an interest on a long-term basis and is jointly controlled by the reporting entity and one or more other venturers under a contractual arrangement”.

As stated in paragraph 140 of the SORP the consortia:

“…arrangements through which participants conduct oil and gas exploration and production operations on a joint basis rarely involve the establishment of a separate entity carrying on a trade of its own. The terms of the joint arrangement are generally set out in a ‘joint operating agreement’ such that all significant matters of operating and financial policy are predetermined. Under the joint operating agreement, the operator is elected to manage the assets and is generally empowered to enter into contracts and incur costs which are rechargeable to the other participants.”

The scope of a joint operating agreement typically covers exploration for, and production of, petroleum, as well as treatment, storage and transportation. It will also cover income allocation, and cost sharing, and the joint venture’s accounting and audit arrangements will normally provide for the appointment one of the participators as “operator”.

The specific features of each joint arrangement should be accounted for according to FRS 9 if UK GAAP is being applied. It is anticipated that the more common arrangements in the oil and gas sector are likely to be considered as JANE in accordance with FRS 9, though they may commonly be referred to as ‘joint ventures’ in the oil and gas industry.

A summary of the nature of the relationship and accounting treatment within the individual entity accounts as described in FRS9 is provided in OT02116.

Tax treatment

For CT purposes ‘joint venture’ activities are treated as part of a company’s business and trading activities and are reflected in the returns and supporting accounts and computations filed by the individual company.

For PRT the tax unit is the individual participator but the scheme is field-based and recognises joint venture activity. For example, Schedule 5 OTA 1975 provides for PRT expenditure relief to be claimed on a field basis by the field “responsible person” on behalf of the joint venture participants. This will normally be the person who has been appointed the operator under the JOA.

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