

UNIT 3: ACCOUNTING STANDARD 27 FINANCIAL REPORTING OF INTERESTS IN JOINT VENTURES

LEARNING OUTCOMES

After studying this unit, you will be able to:

- ◆ Define 'Joint venture' 'joint Control', 'control', 'venturer' and investor.
- ◆ Appreciate different forms of joint venture
- ◆ Examine the contractual arrangements which will differentiate the control as of Associate or Joint venture
- ◆ Evaluate the nitty-gritty of different forms of Joint ventures and differentiate among them
- ◆ Present the separate and consolidated financial statements of the venturers
- ◆ Accounting for transactions between the venturer and Joint venture
- ◆ Comply with the disclosure requirements as stated in the standard.



3.1 INTRODUCTION

You would have come across many examples where 2 or more entities would have worked together to achieve a certain purpose. Hindustan Unilever Ltd (HUL), Tata Starbucks Ltd, Tata SIA Airlines Ltd. (Vistara), etc. are a few popular examples of Joint Ventures. Entities enter into such arrangements considering sharing of risk and expense, collaboration of know-how and skill-set, while also impacted by different work-cultures and management style. Depending on the contractual arrangement, the accounting and reporting for Joint Ventures is done.

AS 27, came into effect in respect of accounting periods commenced on or after 01.04.2002. This standard set out principles and procedures for accounting of interests in joint venture and 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.

The standard deals with three broad types of joint ventures –

1. Jointly controlled operations,
2. Jointly controlled assets and
3. Jointly controlled entities.

The requirements relating to accounting for joint ventures in consolidated financial statements according to proportionate consolidation method, as contained in AS 27, apply only when consolidated financial statements are prepared by venturer. Similarly 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). An investor in joint venture, which does not have joint control, should report its interest in a joint venture in its consolidated financial statements in accordance with AS 13, AS 21 and AS 23.



3.2 SCOPE

This Standard 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.

The provisions of this AS need to be referred to for consolidated financial statement only when CFS is prepared and presented by the venturer.



3.3 DEFINITIONS

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

From the above definition we conclude that the essential conditions for any business relation to qualify as joint venture are:

- ♦ **Two or more parties coming together:** Parties can be an individual or any form of business organization say, BOI, AOP, Company, firm.

- ♦ **Venturers undertake some economic activity:** Economic activity means activities with the profit-making motive. Joint venture is separate from the regular identity of the venturers, it may be in the form of independent and separate legal organization other than regular concern of the venturer engaged in the economic activity.
 - ♦ **Venturers have joint control on the economic activity:** The operating and financial decisions are influenced by the venturers and they also share the results of the economic activity.
 - ♦ **There exists a contractual agreement:** The relationship between venturers is governed by the contractual agreement. This agreement can be in the form of written and signed agreement or as minutes of venturer meeting or in any other written form.
2. **Joint control** is the contractually agreed sharing of control over an economic activity.
 3. **Control** is the power to govern the financial and operating policies of an economic activity so as to obtain benefits from it.
 4. A **venturer** is a party to a joint venture and has joint control over that joint venture.
 5. An **investor** in a joint venture is a party to a joint venture and does not have joint control over that joint venture.
 6. 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.



3.4 CONTRACTUAL ARRANGEMENT

The joint venture covered under this statement is governed on the basis of contractual agreement. Non-existence of contractual agreement will disqualify an organization to be covered in AS 27. Joint ventures with contractual agreement will be excluded from the scope of AS 27 only if the investment qualifies as subsidiary under AS 21, in this case, it will be covered by AS 21. Contractual agreement can be in the form of written contract, minutes of discussion between

parties (venturers), articles of the concern or by-laws of the relevant joint venture.

Irrespective of the form of the contract, the content of the contract ideally should include the following points:

- ◆ The activity, duration and reporting obligations of the joint venture.
- ◆ The appointment of the board of directors or equivalent governing body of the joint venture and the voting rights of the venturers.
- ◆ Capital contributions by the venturers.
- ◆ The sharing by the venturers of the output, income, expenses or results of the joint venture.

The main object of contractual agreement is to distribute the economic control among the venturers, it ensures that no venturer should have unilateral control. 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. If contractual agreement is signed by a party to safeguard its right, such agreement will not make the party a venturer.

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

Example 1

IDBI gave loan to the joint venture entity of L&T and Tania Construction, they signed an agreement according to which IDBI will be informed for all important decisions of the joint venture entity. This agreement is to protect the right of the IDBI, hence just signing the contractual agreement will not make investor a venturer.

Example 2

X Ltd invested ₹ 200 crore as initial capital along with Y Ltd and Z Ltd in GFH Ltd. The purpose of X Ltd making this investment is to grow the business of GFH Ltd along with the other investors. All investors have a right to attend to the meetings

and to take decisions with respect to the business of GFH Ltd. All investors are actively involved in running the business of GFH Ltd and have a share in the returns generated by GFH Ltd in an agreed proportion.

GFH Ltd is an example of a Joint Venture and X Ltd, Y Ltd and Z Ltd are all Venturers.

Similarly, just because contractual agreement has assigned the role of a manager to any of the venturer will not disqualify him as venturer.

Example 3

Mr. A, M/s. B & Co. and C Ltd. entered into a joint venture, where according to the agreement, all the policies making decisions on financial and operating activities will be taken in a regular meeting attended by them or their representatives. Implementation and execution of these policies will be the responsibility of Mr. A. Here Mr. A is acting as venturer as well as manager of the concern.



3.5 FORMS OF JOINT VENTURES

Joint ventures may take many forms and structures, this Statement identifies them in three broad types –

- **Jointly Controlled Operations (JCO),**
- **Jointly Controlled Assets (JCA) and**
- **Jointly Controlled Entities (JCE).**

Any structure which satisfies the following characteristics can be classified as joint ventures:

- (a) Two or more venturers are bound by a contractual arrangement and
- (b) The contractual arrangement establishes joint control.



3.6 JOINTLY CONTROLLED OPERATIONS (JCO)

Under this set up, venturers do not create a separate entity for their joint venture business but they use their own resources for the purpose. They raise any funds required for joint venture on their own, they incur any expenses and sales are also realised individually. They use same set of assets and employees for joint venture business and their own business. 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.

Since there is no separate legal entity and venturers don't recognize the transactions separately, they do not maintain a separate set of books for joint venture. All the transactions of joint venture are recorded in their books only.

Following are the key features of JCO:

- a. Each venturer has his own separate business.
- b. There is no separate entity for joint venture business.
- c. All venturers are creating their own assets and maintain them.
- d. Each venturer record only his own transactions without any separate set of books maintained for the joint venture business.
- e. There is a common agreement between all of them.
- f. Venturers use their assets for the joint venture business.
- g. Venturers met the liabilities created by them for the joint venture business.
- h. Venturers met the expenses of the joint venture business from their funds.
- i. Any revenue generated or income earned from the joint venture is shared by the venturers as per the contract.

Since the jointly controlled operation is not purchasing assets or raising finance in its own right, the assets and liabilities used in the activities of the joint venture are those of the ventures. As such, they are accounted for in the financial statements of the venture to which they belong. The only accounting issue that arises is that the output from the project is to be shared among the venturers and, therefore, there must be some mechanism for specifying the allocation of the proceeds and the sharing of any joint expenses.

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.

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.

Example 4

Mr. A (dealer in tiles and marbles), Mr. B (dealer in various building materials) and Mr. C (Promoter) enters into a joint venture business, where any contract for construction received will be completed jointly, say, Mr. A will supply all tiles and marbles, Mr. B will supply other materials from his godown and Mr. C will look after the completion of construction. As per the contractual agreement, they will share any profit/loss in a predetermined ratio. None of them are using separate staff or other resources for the joint venture business and neither do they maintain a separate account. Everything is recorded in their personal business only.

Venturer doesn't maintain a separate set of books but they record only their own transactions of the joint venture business in their books. Any transaction of joint venture recorded separately is only for internal reporting purpose. Once all transactions recorded in venturer financial statement, they don't need to be adjusted for in consolidated financial adjustment.

Illustration 1

Mr. A, Mr. B and Mr. C entered into a joint venture to purchase a land, construct and sell flats. Mr. A purchased a land for ₹ 60,00,000 on 01.01.20X1 and for the purpose he took loan from a bank for ₹ 50,00,000 @ 8% interest p.a. He also paid registering fees ₹ 60,000 on the same day. Mr. B supplied the materials for ₹ 4,50,000 from his godown and further he purchased the materials for ₹ 5,00,000 for the joint venture. Mr. C met all other expenses of advertising, labour and other incidental expenses which turnout to be ₹ 9,00,000. On 30.06.20X1 each of the venturer agreed to take away one flat each to be valued at ₹ 10,00,000 each flat and rest were sold by them as follow: Mr. A for ₹ 40,00,000; Mr. B for ₹ 20,00,000 and Mr. C for ₹ 10,00,000. Loan was repaid on the same day by Mr. A along with the interest and net proceeds were shared by the partners equally.

You are required to prepare the draft Consolidated Profit & Loss Account and Joint Venture Account in the books of each venturer.

Solution

Draft Consolidated Profit & Loss Account

Particulars	₹	₹	Particulars	₹	₹
To Purchase of Land:			By Sale of Flats:		
Mr. A		60,00,000	Mr. A	40,00,000	
To Registration Fees:			Mr. B	20,00,000	
Mr. A		60,000	Mr. C	<u>10,00,000</u>	70,00,000
To Materials:			By Flats taken by Venturers:		
Mr. B		9,50,000	Mr. A	10,00,000	
To Other Expenses:			Mr. B	10,00,000	
Mr. C		9,00,000	Mr. C	<u>10,00,000</u>	30,00,000
To Bank Interest:					
Mr. A		2,00,000			
To Profits:					
Mr. A	6,30,000				
Mr. B	6,30,000				
Mr. C	<u>6,30,000</u>	<u>18,90,000</u>			
		<u>1,00,00,000</u>			<u>1,00,00,000</u>

**In the Books of Mr. A
Joint Venture Account**

Particulars	₹	Particulars	₹
To Bank Loan (Purchase of Land)	50,00,000	By Bank (Sale of Flats)	40,00,000
To Bank:(Purchase of Land)	10,00,000	By Land & Building	10,00,000
To Bank (Registration Fees)	60,000	By Bank (Received from Mr. B)	14,20,000
To Bank (Bank Interest)	2,00,000	By Bank (Received from Mr. C)	4,70,000
To Profit on JV	<u>6,30,000</u>		<u> </u>
	<u>68,90,000</u>		<u>68,90,000</u>

**In the Books of Mr. B
Joint Venture Account**

Particulars	₹	Particulars	₹
To Purchases (Material Supplied)	4,50,000	By Bank (Sale of Flats)	20,00,000
To Bank (Materials)	5,00,000	By Land & Building	10,00,000
To Profit on JV	6,30,000		
To Bank (Paid to Mr. A)	<u>14,20,000</u>		<u> </u>
	<u>30,00,000</u>		<u>30,00,000</u>

**In the Books of Mr. C
Joint Venture Account**

Particulars	₹	Particulars	₹
To Bank (Misc. Expenses)	9,00,000	By Bank (Sale of Flats)	10,00,000
To Profit on JV	6,30,000	By Land & Building	10,00,000
To Bank (Paid to Mr. A)	<u>4,70,000</u>		<u> </u>
	<u>20,00,000</u>		<u>20,00,000</u>



3.7 JOINTLY CONTROLLED ASSETS (JCA)

Separate legal entity is not created in this form of joint venture but venturer owns the assets jointly, which are used by them for the purpose of generating economic benefit to each of them. They take up any expenses and liabilities related to the joint assets as per the contract. We can conclude the following points:

- ◆ There is no separate legal identity.
- ◆ There is a common control over the joint assets.
- ◆ Venturers use this asset to derive some economic benefit to themselves.
- ◆ Each venturer incurs separate expenses for their transactions.
- ◆ Expenses on jointly held assets are shared by the venturers as per the contract.
- ◆ In their financial statement, venturer shows only their share of the asset and total income earned by them along with total expenses incurred by them.
- ◆ Since 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.
- ◆ 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.

Example 5

ABC Ltd., BP Ltd. and HP Ltd. having the same point of oil refinery and same place of customers agreed to spread a pipeline from their unit to customers place jointly. They agreed to share the expenditure on the pipeline construction and maintenance in the ratio 3:3:4 respectively and the time allotted to use the pipeline was in the ratio 4:3:3 respectively.

*For the joint venture, each venturer will record his share of joint assets as **classified according to the nature of the assets rather than as an investment** and any expenditure incurred or revenue generated will be recorded with other items similar to JCO.*

Following are the few differences between JCO and JCA for better understanding:

- ♦ In JCO, venturers use their own assets for joint venture business but in JCA they jointly own the assets to be used in joint venture.
- ♦ JCO is an agreement to joint carry on the operations to earn income whereas, JCA is an agreement to jointly construct and maintain an asset to generate revenue to each venturer.
- ♦ Under JCO all expenses and revenues are shared at an agreed ratio, in JCA only expenses on joint assets are shared at the agreed ratio.

Illustration 2

A Ltd., B Ltd. and C Ltd. decided to jointly construct a pipeline to transport the gas from one place to another that was manufactured by them. For the purpose following expenditure was incurred by them: Buildings ₹ 12,00,000 to be depreciated @ 5% p.a., Pipeline for ₹ 60,00,000 to be depreciated @ 15% p.a., computers and other electronics for ₹ 3,00,000 to be depreciated @ 40% p.a. and various vehicles of ₹ 9,00,000 to be depreciated @ 20% p.a.

They also decided to equally bear the total expenditure incurred on the maintenance of the pipeline that comes to ₹ 6,00,000 each year.

You are required to show the consolidated balance sheet and the extract of Statement of Profit & Loss and Balance Sheet for each venturer.

Solution

Consolidated Balance Sheet

		Note	(₹)
I	Equity and liabilities		
	Shareholders' funds:		
	Share Capital	1	<u>71,40,000</u>
			<u>71,40,000</u>
II	Assets		
	Non-current Assets		
	Property, Plant and Equipment:	2	<u>71,40,000</u>
			<u>71,40,000</u>

Notes to Accounts

			(₹)
1.	Share capital		
	A Ltd.	23,80,000	
	B Ltd.	23,80,000	
	C Ltd.	23,80,000	71,40,000
2.	Property, Plant and Equipment		
	Land & Building:		
	A Ltd.	3,80,000	
	B Ltd.	3,80,000	
	C Ltd.	<u>3,80,000</u>	11,40,000
	Plant & Machinery:		
	A Ltd.	17,00,000	
	B Ltd.	17,00,000	
	C Ltd.	<u>17,00,000</u>	51,00,000
	Computers:		
	A Ltd.	60,000	
	B Ltd.	60,000	
	C Ltd.	<u>60,000</u>	1,80,000
	Vehicles:		
	A Ltd.	2,40,000	
	B Ltd.	2,40,000	
	C Ltd.	<u>2,40,000</u>	<u>7,20,000</u>

**In the Books of A Ltd.
Extract of statement of Profit & Loss**

Particulars	Note No.	₹
Depreciation and amortisation expense	1	4,20,000
Other operating Expenses (Pipeline Expenses)		200,000

Extract of Balance Sheet

	Note No.	₹
<i>Assets</i>		
Non-current assets		
Property, Plant and Equipment	2	23,80,000

Notes to Accounts

		₹	₹
1.	Depreciation and amortisation expense		
	Land & Building	20,000	
	Plant & Machinery	3,00,000	
	Computers	40,000	
	Vehicles	<u>60,000</u>	4,20,000
2.	Land & Building	4,00,000	
	Less: Depreciation	<u>(20,000)</u>	3,80,000
	Plant & Machinery	20,00,000	
	Less: Depreciation	<u>(3,00,000)</u>	17,00,000
	Computers	1,00,000	
	Less: Depreciation	<u>(40,000)</u>	60,000
	Vehicles	3,00,000	
	Less: Depreciation	<u>(60,000)</u>	<u>2,40,000</u>
			<u>23,80,000</u>

In the Books of B Ltd.
Extract of draft Profit & Loss Account

Particulars	Note No.	₹
Depreciation and amortisation expense	1	4,20,000
Other operating Expenses (Pipeline Expenses)		200,000

Extract of Balance Sheet

	Note No.	₹
Assets		
Non-current assets		
Property, Plant and Equipment	2	23,80,000

Notes to Accounts

		₹	₹
1.	Depreciation and amortisation expense		
	Land & Building	20,000	
	Plant & Machinery	3,00,000	
	Computers	40,000	
	Vehicles	<u>60,000</u>	4,20,000
2.	Land & Building	4,00,000	
	Less: Depreciation	<u>(20,000)</u>	3,80,000
	Plant & Machinery	20,00,000	
	Less: Depreciation	<u>(3,00,000)</u>	17,00,000
	Computers	1,00,000	
	Less: Depreciation	<u>(40,000)</u>	60,000
	Vehicles	3,00,000	
	Less: Depreciation	<u>(60,000)</u>	<u>2,40,000</u>
			<u>23,80,000</u>

In the Books of C Ltd.

Extract of Draft Profit & Loss Account	Note No.	₹
Depreciation and amortisation expense	1	4,20,000
Other operating Expenses (Pipeline Expenses)		200,000

Extract of Balance Sheet

	Note No.	₹
<i>Assets</i>		
Non-current assets		
Property, Plant and Equipment	2	23,80,000

Notes to Accounts

		₹	₹
1.	Depreciation and amortisation expense		
	Land & Building	20,000	
	Plant & Machinery	3,00,000	
	Computers	40,000	
	Vehicles	<u>60,000</u>	4,20,000
2.	Land & Building	4,00,000	
	Less: Depreciation	<u>(20,000)</u>	3,80,000
	Plant & Machinery	20,00,000	
	Less: Depreciation	<u>(3,00,000)</u>	17,00,000
	Computers	1,00,000	
	Less: Depreciation	<u>(40,000)</u>	60,000
	Vehicles	3,00,000	
	Less: Depreciation	<u>(60,000)</u>	<u>2,40,000</u>
			<u>23,80,000</u>



3.8 JOINTLY CONTROLLED ENTITIES (JCE)

This is the format where venturer creates a new entity for their joint venture business. 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. All the venturers pool their resources under new banner and this entity purchases its own assets, create its own liabilities, expenses are incurred by the entity itself and sales are also made by this entity. The net result of the entity is shared by the venturers in the ratio agreed upon in the contractual agreement. This contractual agreement also determines the joint control of the venturer. 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.

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

Example

A Ltd and B Ltd are two infrastructure companies operating in City A. The local authority has issued a tender to construct a metro stretch for ₹ 2,000 crore and had invited bidders to apply for the tender. A Ltd and B Ltd, jointly form a new entity AB Ltd that bids for the tender. All machinery and equipment will be the responsibility of A Ltd. All funding will be managed and controlled by B Ltd. Revenue and operating expenses will be shared jointly by A Ltd and B Ltd in the proportion of 60:40.

In the above example AB Ltd constitutes a Jointly Controlled Entity (JCE).

Example (Jointly Controlled Entity (JCE))

Three separate aerospace companies form a separate entity, Aero Ltd, to jointly manufacture an aircraft. They carry responsibility for different areas of expertise, such as: manufacturing engines; manufacturing fuselage and wings; and aerodynamics.

The companies carry out different parts of the manufacturing process, each using its own resources and expertise in order to manufacture, market and distribute the aircraft jointly. The three entities share the revenues from the sale of aircraft and jointly incur expenses.

The revenues and common costs are shared, as agreed in the consortium contract. Parties also incur their own separate costs, such as labour costs, manufacturing costs, supplies, inventory of unused parts and work in progress. Each party recognises its separately incurred costs in full.

Aero Ltd maintains separate accounting records. The consortium agreement comprises the following:

Aero Ltd will invoice the customers on the investors' behalf. The allocation of revenue from the aircraft's sale is in proportion to the investors' interests.

All administrative costs incurred by Aero Ltd are shared by the parties in proportion to their interests; Aero Ltd will recharge these, with no additional margin.

The companies carry out different parts of the manufacturing process, each using its own resources and expertise to manufacture, market and distribute the aircraft jointly.

Each company incurs its own separate costs, such as labour costs, manufacturing costs, supplies, inventory of unused parts and work in progress. Each company recognises its separately incurred costs in full.

Being a separate entity, separate set of books is maintained for the joint venture and in the individual books of venturers the investment in joint venture is recorded as investment (AS 13). Joint venture can be a foreign company operating in India through an Indian concern say Gremo Insurance of Germany contributes 49% of the assets in joint venture in India with Indo Bank Ltd. of India. They agreed to share the net results in 1:1 ratio. The main objective of the joint venture is to exploit the technical expertise of Gremo Insurance and Goodwill of Indo Bank Ltd. It can also be two or more local concerns opening an organization or firm or company contributing their assets to this new joint venture concern and share the profits of the operation in the agreed ratio.

Illustration 3

A Ltd. a UK based company entered into a joint venture with B Ltd. in India, wherein B Ltd. will import the goods manufactured by A Ltd. on account of joint venture and sell them in India. A Ltd. and B Ltd. agreed to share the expenses & revenues in the ratio of 5:4 respectively whereas profits are distributed equally. A Ltd. invested 49% of total capital but has equal share in all the assets and is equally liable for all the liabilities of the joint venture. Following is the trial balance of the joint venture at the end of the first year:

Particulars	Dr. (₹)	Cr. (₹)
Purchases	9,00,000	
Other Expenses	3,06,000	
Sales		13,05,000
Property, Plant and Equipment	6,00,000	
Current Assets	2,00,000	
Unsecured Loans		2,00,000
Current Liabilities		1,00,000
Capital		4,01,000

Closing inventory was valued at ₹ 1,00,000.

You are required to prepare the Consolidated Financial Statement.

Solution**Consolidated Profit & Loss Account**

Particulars	Note No.	(₹)
Revenue from operations	1	<u>13,05,000</u>
Total Revenue (A)		<u>13,05,000</u>
Less: Expenses		
Purchases	2	9,00,000
Other expenses	3	3,06,000

Changes in inventories of finished goods	4	<u>(1,00,000)</u>
Total Expenses (B)		<u>11,06,000</u>
Profit Before Tax (A-B)		<u>1,99,000</u>

Consolidated Balance Sheet

		Note No.	(₹)
I	Equity and liabilities		
	1. Shareholders' funds:		
	Share Capital	5	4,01,000
	Reserves and Surplus	6	1,99,000
	2. Non-current liabilities		
	Long term borrowings	7	2,00,000
	3. Current Liabilities	8	<u>1,00,000</u>
			<u>9,00,000</u>
II	Assets		
	Non-current Assets		
	Property, Plant and Equipment	9	6,00,000
	Current Assets		
	Inventories	10	1,00,000
	Other current assets	11	<u>2,00,000</u>
			<u>9,00,000</u>

Notes to Accounts

	Particulars		(₹)
1.	Revenue from operations		
	Sales:		
	A Ltd.	7,25,000	
	B Ltd.	<u>5,80,000</u>	13,05,000

2.	Purchases		
	A Ltd.	5,00,000	
	B Ltd.	<u>4,00,000</u>	9,00,000
3.	Other expenses		
	A Ltd.	1,70,000	
	B Ltd.	<u>1,36,000</u>	3,06,000
4.	Closing Inventory		
	A Ltd.	50,000	
	B Ltd.	<u>50,000</u>	1,00,000
5.	Share Capital		
	A Ltd.	1,96,490	
	B Ltd.	<u>2,04,510</u>	4,01,000
6.	Reserves and Surplus		
	Profit & Loss Account:		
	A Ltd.	99,500	
	B Ltd.	<u>99,500</u>	1,99,000
7.	Long Term Borrowings		
	Unsecured Loans:		
	A Ltd.	1,00,000	
	B Ltd.	<u>1,00,000</u>	2,00,000
8.	Current Liabilities		
	A Ltd.	50,000	
	B Ltd.	<u>50,000</u>	1,00,000
9.	Property, Plant and Equipment		
	A Ltd.	3,00,000	
	B Ltd.	<u>3,00,000</u>	6,00,000

10. Inventories			
A Ltd.	50,000		
B Ltd.	<u>50,000</u>	1,00,000	
11. Other Current Assets			
A Ltd.	1,00,000		
B Ltd.	<u>1,00,000</u>	2,00,000	



3.9 CONSOLIDATED FINANCIAL STATEMENTS OF A VENTURER

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.

Proportionate consolidation method of accounting is to be followed except in the following cases:

- Investment is intended to be temporary because the investment is acquired and held exclusively with a view to its subsequent disposal in the near future. And
- joint venture operates under severe long-term restrictions, which significantly impair its ability to transfer funds to the venturers.

In both the above cases, investment of venturer in the share of the investee is treated as investment according to AS 13.

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

- It ceases to have joint control in the joint venture but retains, either in whole or in part, its investment.
- The use of the proportionate consolidation method is no longer appropriate because the joint venture operates under severe long-term restrictions that significantly impair its ability to transfer funds to the venturers.

From the date of discontinuing the use of the proportionate consolidation method,

- a. If interest in entity is more than 50%, investments in such joint ventures should be accounted for in accordance with AS 21, Consolidated Financial Statement.
- b. If interest is 20% or more but upto 50%, investments are to be accounted for in accordance with AS 23, Accounting for Investment in Associates in Consolidated Financial Statement.
- c. For all other cases investment in joint venture is treated as per AS 13, Accounting for Investment.
- d. For this purpose, the carrying amount of the investment at the date on which joint venture relationship ceases to exist should be regarded as cost thereafter.

Following are the features of Proportionate Consolidation Method:

- a. Stress is given on substance over form i.e., more importance is given to the share of venturers in the profit or loss of the venture from the share of assets and liabilities rather than the nature and form of the joint venture.
- b. Venturer's share of joint assets, liabilities, expenses and income are shown on the separate lines in the consolidated financial statement.

For example, Mr. A enters into a joint venture with Mr. B and has contributed 33% of the total Property, Plant and Equipment and has share of 40% in current assets and current liabilities. Its share in net result is 50%. Consolidated Balance Sheet will be prepared by Mr. A as follow:

Consolidated Balance Sheet

		Note No.	(₹)
I	Equity and liabilities		
	1. Shareholders' funds:		
	Share Capital	1	1,00,000
	2. Current Liabilities	2	<u>50,000</u>
			<u>1,50,000</u>

II	Assets		
	Non-current Assets		
	Property, Plant and Equipment	3	75,000
	Current Assets	4	<u>75,000</u>
			<u>1,50,000</u>

Notes to Accounts

1.	Share Capital *:		
	A (25,000 + 30,000 - 20,000)	35,000	
	B (50,000 + 45,000 - 30,000)	<u>65,000</u>	1,00,000
2.	Current Liabilities:		
	A	20,000	
	B	<u>30,000</u>	50,000
3.	Property, Plant and Equipment:		
	A	25,000	
	B	<u>50,000</u>	75,000
4.	Current Assets:		
	A	30,000	
	B	<u>45,000</u>	75,000

* Contribution to Share capital taken as a balancing figure in absence of information in this regard in the example

Similar to above all the items of expenses and income will also be classified line by line for each item. The whole basis of this provision is to bring transparency in the books of account. If there is any special clause for sharing of expenses, income or any other item that should be clearly disclosed in the consolidated financial statement.

- c. Most of the provisions of Proportionate Consolidation Method are similar to the provisions of AS 21.

- d. As far as possible the reporting date of the financial statements of jointly controlled entity and venturers should be same. If practically it is not possible to draw up the financial statements to such date and, accordingly, those financial statements are drawn up to different reporting dates, adjustments should be made in joint venturer's books for the effects of significant transactions or other events that occur between the jointly controlled entity's date and the date of the venturer's financial statements. In any case, the difference between reporting dates should not be more than six months.
- e. Accounting policies followed in the preparation of the financial statements of the jointly controlled entity and venturer should be uniform for like transactions and other events in similar circumstances.

If accounting policies followed by venturer and jointly controlled entity are not uniform, then adjustments should be made in the items of the venturer to bring it in line with the accounting policy of the joint venture.
- f. Any asset or liability should not be adjusted by another liability or asset. Similarly any income or expense cannot be adjusted with another expense or income. Such adjustment can be made only when legally it is allowed to adjust them and such items does lead to settlement of obligation or writing off of assets.
- g. On the date when interest in joint entity is acquired, if the interest of venturer in net assets of the entity is less than the cost of investment in joint entity, the difference will be recognized as goodwill in the consolidated financial statement and if net asset is more than cost of investment, then the difference is recognized as capital reserve.

In case the carrying amount of investment is different than cost of investment, we take carrying amount for the purpose of the above calculation.
- h. An investor who don't have joint control in the entity is like associate as discussed in AS 23, therefore the treatment of losses will be similar to AS 23. If investor's share in loss of the joint entity is in excess of his interest in net asset, this excess loss will be recognized by the venturers. In future when entity starts reporting profits, investor's share of profits will be provided to venturer till total amount is equivalent to absorbed losses.

Illustration 4

A Ltd. entered into a joint venture with B Ltd. on 1:1 basis and a new company C Ltd. was formed for the same purpose and following is the balance sheet of all the three companies:

Particulars	A Ltd.	B Ltd.	C Ltd.
Share Capital	10,00,000	7,50,000	5,00,000
Reserve & Surplus	18,00,000	16,00,000	12,00,000
Loans	3,00,000	4,00,000	2,00,000
Current Liabilities	4,00,000	2,50,000	1,00,000
Property, Plant and Equipment	30,50,000	26,25,000	19,50,000
Investment in JV	2,50,000	2,50,000	-
Current Assets	2,00,000	1,25,000	50,000

Prepare the balance sheet of A Ltd. and B Ltd. under proportionate consolidation method.

Solution

Balance Sheet of A Ltd.

		Note No.	(₹)
I	Equity and liabilities		
	1. Shareholders' funds:		
	Share Capital		10,00,000
	Reserves and Surplus	1	24,00,000
	2. Non-current liabilities	2	4,00,000
	3. Current Liabilities	3	<u>4,50,000</u>
	TOTAL		<u>42,50,000</u>

II	Assets		
	Non-current Assets		
	Property, Plant and Equipment:	4	40,25,000
	Current Assets	5	<u>2,25,000</u>
			<u>42,50,000</u>

Notes to Accounts

		₹	₹
1.	Reserves and Surplus		
	A Ltd.	18,00,000	
	C Ltd.	<u>6,00,000</u>	24,00,000
2.	Long Term Borrowings		
	Loans:		
	A Ltd.	3,00,000	
	C Ltd.	<u>1,00,000</u>	4,00,000
3.	Current Liabilities:		
	A Ltd.	4,00,000	
	C Ltd.	<u>50,000</u>	4,50,000
4.	Property, Plant and Equipment:		
	A Ltd.	30,50,000	
	C Ltd.	<u>9,75,000</u>	40,25,000
5.	Current Assets:		
	A Ltd.	2,00,000	
	C Ltd.	<u>25,000</u>	2,25,000

Balance Sheet of B Ltd.

		Note No.	(₹)
I	Equity and liabilities		
	1. Shareholders' funds:		
	Share Capital		7,50,000
	Reserves and Surplus	1	22,00,000
	2. Non-current liabilities	2	5,00,000
	3. Current Liabilities	3	<u>3,00,000</u>
			<u>37,50,000</u>

II	Assets		
	1. Non-current Assets		
	Property, Plant and Equipment	4	36,00,000
	2. Current Assets	5	
			<u>1,50,000</u>
			<u>37,50,000</u>

Notes to Accounts

		₹	₹
1.	Reserves and Surplus		
	A Ltd.	16,00,000	
	C Ltd.	<u>6,00,000</u>	22,00,000
2.	Long Term Borrowings		
	Loans:		
	A Ltd.	4,00,000	
	C Ltd.	<u>1,00,000</u>	5,00,000
3.	Current Liabilities:		
	A Ltd.	2,50,000	
	C Ltd.	<u>50,000</u>	3,00,000
4.	Property, Plant and Equipment:		
	A Ltd.	26,25,000	
	C Ltd.	<u>9,75,000</u>	36,00,000
5.	Current Assets:		
	A Ltd.	1,25,000	
	C Ltd.	25,000	1,50,000



3.10 TRANSACTIONS BETWEEN A VENTURER AND JOINT VENTURE

When venturer transfers or sells assets to Joint Venture, 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 only when the contribution or sale provides evidence of a reduction in the net realisable value of current assets or an impairment loss.

When the venturer from the joint venture purchases the assets, venturer will not recognize his share of profits in the joint venture of such transaction unless he disposes off the assets. A venturer should recognise his share of the losses resulting from these transactions in the same way as profits except that losses will be recognised in full immediately only when they represent a reduction in the net realisable value of current assets or an impairment loss.

In case the joint venture is in the form of separate entity (i.e., JCE) then provisions of above the Para will be followed only for consolidated financial statement and not for venturer's own financial statement. In the books of venturer, profit or loss from such transactions are recognised in full.

Example

A and B established a separate vehicle i.e. entity J, wherein each operator has a 50% ownership interest and each takes 50% of the output. On formation of the joint venture, A contributed a property with fair value of ₹ 110 crore and agreed to contribute his experience over the years towards this venture; and B contributed equipment with a fair value of ₹ 120 crore. The carrying values of the contributed assets were ₹ 100 crore and ₹ 80 crore, respectively.

Answer

A – Gain in consolidated financial statements

A's share in the fair value of assets contributed by entity

<i>B (50% × 120)</i>	<i>60</i>
----------------------	-----------

A's share in the carrying value of asset contributed by

<i>A to the joint venture (50% × 100)</i>	<i>(50)</i>
---	-------------

<i>Gain recognised by A</i>	<i>10</i>
-----------------------------	-----------



3.11 REPORTING INTERESTS IN JOINT VENTURES IN THE FINANCIAL STATEMENTS OF AN INVESTOR

The investors who don't have joint control over the entity recognized his share of net results and his investments in joint venture as per AS 13. In the consolidated financial statement it is recognized as per AS 13, AS 21 or AS 23 as appropriate.



3.12 OPERATORS OF JOINT VENTURES

Payment to operators is recognized as expense in CFS and in the books of the operators as per AS 9, Revenue Recognition. The operator may be any of the venturers, in this case any amount received by him, as management fees for the service will be recognized as stated above in this Para.



3.13 DISCLOSURE

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.

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.

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. 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.

Reference: The students are advised to refer the full text of AS 27 "Financial Reporting of Interests in Joint Ventures"

TEST YOUR KNOWLEDGE

MCQs

1. State which of the following statements are incorrect.
 - (i) The requirements relating to accounting for joint ventures in consolidated financial statements according to proportionate consolidation method, as contained in AS 27, applies only when consolidated financial statements are prepared by venturer.
 - (ii) The requirements relating to accounting for joint ventures in consolidated financial statements according to proportionate consolidation method, as contained in AS 27, applies irrespective whether consolidated financial statements are prepared by venturer or not.
 - (iii) An investor in joint venture, which does not have joint control, should report its interest in a joint venture in its consolidated financial statements in accordance with AS 13, AS 21 and AS 23 as the case may be.
 - (a) Point (i) is incorrect.
 - (b) Point (ii) is incorrect.
 - (c) Point (iii) is incorrect.
 - (d) None of the above.
2. Identify which of the following is not a feature of a Jointly controlled operations (JCO):
 - a. Each venturer has his own separate business.
 - b. There is a separate entity for joint venture business.
 - c. Each venturer record only his own transactions without any separately set of books maintained for the joint venture business.
 - d. There is a common agreement between all of them.
3. Identify which of the following is/are not a feature of a Jointly controlled assets (JCA):

- (i) *There is a separate legal identity.*
 - (ii) *There is a common control over the joint assets.*
 - (iii) *Expenses on jointly held assets are shared by the venturers as per the contract.*
 - (iv) *In their financial statement, venturer shows only their share of the asset and total income earned by them along with total expenses incurred by them.*
 - (a) *Point no. (i) only.*
 - (b) *Point no. (i) and (iii).*
 - (c) *Point no. (iii) and (iv).*
 - (d) *Point (i) and (ii).*
4. *Identify which is/ are features of a Jointly controlled entity (JCE):*
- (i) *Venturer creates a new entity for their joint venture business.*
 - (ii) *All the venturers pool their resources under new banner and this entity purchases its own assets, create its own liabilities, expenses are incurred by the entity itself and sales are also made by this entity.*
 - (iii) *The revenues and expenses of the entity is shared by the venturers in the ratio agreed upon in the contractual agreement.*
 - (a) *Point no. (i) only.*
 - (b) *Point no. (i) and (ii).*
 - (c) *Point no. (iii).*
 - (d) *Point no. (iii).*
5. *Identify the correct statements.*
- From the date of discontinuing the use of the proportionate consolidation method:*

- (i) *If interest in entity is more than 50%, investments in such joint ventures should be accounted for in accordance with AS 21, Consolidated Financial Statements.*
- (ii) *If interest is 20% or more but upto 50%, investments are to be accounted for in accordance with AS 23, Accounting for Investment in Associates in Consolidated Financial Statements.*
- (iii) *For all other cases investment in joint venture is treated as per AS 13, Accounting for Investments.*
- (iv) *For this purpose, the fair value of the investment at the date on which joint venture relationship ceases to exist should be regarded as cost thereafter.*
 - (a) *Point no. 1 and 2.*
 - (b) *Point no. 1, 2 and 3.*
 - (c) *Point no. 1, 2, 3 and 4.*
 - (d) *None of the above.*

Theory Questions

- 6. *Describe the cases when AS 27 does not allow the use of Proportionate consolidation method of accounting?*
- 7. *When is a venturer required to discontinue the use of the proportionate consolidation method?*

Practical Question

- 8. *JVR Limited has made investments of ₹ 97.84 crores in equity shares of QSR Limited in pursuance of Joint Venture agreement till 20X1-X2 (i.e., more than 12 months). The investment has been made at par. QSR Limited has been in continuous losses for the last 2 years. JVR Limited is willing to reassess the carrying amount of its investment in QSR Limited and wish to provide for diminution in value of investments. However, QSR Limited has a futuristic and profitable business plans and projection for the coming years. Discuss whether the contention of JVR Limited to bring down the carrying amount of investment in QSR Limited is in accordance with the Accounting Standard.*

ANSWERS/SOLUTION

MCQs

1.	(b)	2.	(b)	3.	(a)	4.	(c)	5.	(b)
----	-----	----	-----	----	-----	----	-------	----	-----

Theory Questions

6. Proportionate consolidation method of accounting is to be followed except in the following cases:

- a. Investment is intended to be temporary because the investment is acquired and held exclusively with a view to its subsequent disposal in the near future.

The term 'Near Future' is explained with AS 21.

Or

- b. joint venture operates under severe long-term restrictions, which significantly impair its ability to transfer funds to the venturers.

In both the above cases, investment of venturer in the share of the investee is treated as investment according to AS 13.

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

- a. It ceases to have joint control in the joint venture but retains, either in whole or in part, its investment.
- b. The use of the proportionate consolidation method is no longer appropriate because the joint venture operates under severe long-term restrictions that significantly impair its ability to transfer funds to the venturers.

From the date of discontinuing the use of the proportionate consolidation method,

- a. If interest in entity is more than 50%, investments in such joint ventures should be accounted for in accordance with AS 21, Consolidated Financial Statement.
- b. If interest is 20% or more but up to 50%, investments are to be accounted for in accordance with AS 23, Accounting for Investment in Associates in Consolidated Financial Statement.

- c. For all other cases investment in joint venture is treated as per AS 13, Accounting for Investment.
- d. For this purpose, the carrying amount of the investment at the date on which joint venture relationship ceases to exist should be regarded as cost thereafter.

Practical Questions

- 8.** As per para 26 of AS 27 "Financial Reporting of Interests in Joint Ventures", in a venturer's separate financial statements, interest in a jointly controlled entity should be accounted for as an investment in accordance with AS 13 'Accounting for Investments'.

As per para 17 of AS 13 "Accounting for Investments", long-term investments are usually carried at cost. However, when there is a decline, other than temporary, in the value of a long-term investment, the carrying amount is reduced to recognize the decline. Indicators of the value of an investment are obtained by reference to its market value, the investee's assets and results and the expected cash flows from the investment. The type and extent of the investor's stake in the investee are also taken into account. However, where there is a decline, other than temporary, in the carrying amounts of long-term investments, the resultant reduction in the carrying amount is charged to the profit and loss statement.

Since the investment was made in the year 20X1-20X2 i.e., more than a year, it is a long-term investment. In the given case, though the QSR Ltd. is in continuous losses for past 2 years, yet it has a futuristic and profitable business plans and projections for the coming years. Here, one of the indicators i.e. 'losses incurred to the company' may lead to diminution in the value of the shares while the other indicator that 'the company has positive expected cash flows from its business plans' does not lead to decline in the value of shares.

Considering both the facts, in case the expectation of profitable business plans and positive cash flows is based reliable presumptions (such as tender in favour of QSR Ltd., strong order book etc.), the decline will be regarded as temporary in nature and the investment in equity shares will continue to be carried at cost only.

However, should the aforesaid presumptions be based on projections without reasonable evidence backing the claims, the decline could be regarded as non-temporary in nature in which case the write down of the carrying amount become necessary in line with AS 13, thereby implying the contention of QSR Ltd. to be correct.

[illegible]

