Technical Accounting Alert

Non-controlling interests and other comprehensive income

Introduction

This alert provides guidance on accounting for items of other comprehensive income (OCI) that relate to subsidiaries in the following circumstances:

- there is a non-controlling interest in the subsidiary;
- the parent's ownership interest increases or decreases (without loss of control); or
- the parent loses control of the subsidiary.

Relevant Australian standards

References in this TA alert are made to standards issued by the International Accounting Standards Board. The Australian equivalent to each standard included in this alert is shown below:

International Standard reference	Australian equivalent standard
IAS 1 *Presentation of Financial Statements*	AASB 101 *Presentation of Financial Statements*
IAS 16 *Property, Plant and Equipment*	AASB 116 *Property, Plant and Equipment*
IAS 21 *The Effect of Changes in Foreign Exchange Rates*	AASB 121 *The Effect of Changes in Foreign Exchange Rates*
IAS 27 *Consolidated Financial Statements*	AASB 127 *Consolidated Financial Statements*
IAS 28 *Investments in Associates*	AASB 128 *Investments in Associates*
IAS 39 *Financial Instruments: Recognition and Measurement*	AASB 139 *Financial Instruments: Recognition and Measurement*
IFRS 3 *Business Combinations*	AASB 3 *Business Combinations*

Overview

OCI when there are non-controlling interests

Items credited or charged to OCI

If items charged or credited to OCI relate to a subsidiary in which there is a non-controlling interest, the current period and cumulative balance is allocated between the parent's ownership interest and the non-controlling interest. In practice this involves:

- recording 100% of the OCI in the single Statement of Comprehensive Income or separate Statement of Other Comprehensive Income
- disclosing the attribution of total comprehensive income between the non-controlling interest and owners of the parent (IAS 1.83(b))
- including the non-controlling interest's share of accumulated OCI in the non-controlling interest's component of equity.

This third requirement has the effect that the components of equity (sometimes referred to as 'reserves') that relate to specific types of OCI do not show 100% of the cumulative OCI in the Statement of Financial Position or in the Statement of Changes in Equity (see example below).

Example 1: Attribution of 'revaluation surplus'

Entity P owns 90% of Entity S with the remaining 10% held by non-controlling interests. Entity P applies the IAS 16 revaluation model in its consolidated financial statements. The revaluation surplus is included as a separate component of equity (or reserve). At 31 December 20X0 Entity S's property is revalued, and a revaluation surplus of $100 arises in the annual period. The cumulative revaluation surplus on S's property at this reporting date is $500.

This has the following effects on Entity P's consolidated financial statements (**ignoring any tax effects**)

- it give rise to current period OCI of $100;
- in the allocation of total comprehensive income, $90 is attributed to the parent's owners and $10 to the non-controlling interests; and
- in the Statement of Financial Position and Statement of Changes in Equity, the revaluation reserve is stated as $450. The remaining revaluation surplus of $50 is included in the non-controlling interest part of equity. (Total equity attributable to non-controlling interests is not typically analysed between its components in published financial statements, hence this amount of $50 may not be visible).

The illustrative presentation included in IAS 1's Implementation Guidance provides a more extensive example along with illustrative primary statements.

Reclassification adjustments

Reclassification adjustments arising on disposal or impairment of available-for-sale financial assets, and adjustments arising from cash flow hedge accounting, relate to 100% of the applicable amount previously recognised in OCI. The OCI reclassified into profit or loss for the period therefore includes both the amounts attributed to the parent's owners and the amounts attributed to the non-controlling interests. Consequently, the total reclassification adjustment presented in the Statement of Comprehensive Income is not the amount included in the applicable component of equity (as this is the amount attributable to the parent's owners). The amount of OCI reclassified to profit or loss that was attributed to the non-controlling interests is reallocated to those interests.

Example 2 - reclassification adjustment

Entity P owns 90% of Entity S with the remaining 10% held by non-controlling interests. At 31 June 20X1 Entity S holds an available-for-sale financial asset at its fair value of $400. Original cost was $300 and the cumulative gain of $100 has been reported in OCI. Of this $100 gain, $90 is included in an AFS reserve within the parent's owners' equity and $10 has been allocated to the non-controlling interest component of equity. On the same day, Entity S sells the asset for its carrying amount of $400.

The accounting entries recorded are:

	Dr	**Cr**
Cash	400	
AFS investment		400
Gain on disposal (P&L)*		100
AFS reserve (equity)	90	
Non-controlling interests (equity)	10	

*The gain on disposal of $100 is itself allocated between the parent's owners and the non-controlling interest as per Example 1 above. The effect on equity is: the $90 that was in the AFS reserve becomes part of retained earnings; non-controlling interests stays the same (as the 10% share of OCI of $10 is removed and the 10% share of the P&L gain is reallocated, the net effect on non-controlling interest is nil).

Reclassification adjustments arising on loss of control are addressed later.

OCI and changes in ownership interests

If the parent's ownership interest in a subsidiary is increased or decreased (without loss of control):

- controlling and non-controlling interests are adjusted to reflect the new relative interests (IAS 27.31). In Grant Thornton’s view, the components of equity relating to cumulative OCI (eg revaluation, currency translation and AFS reserves) should be reallocated between the amounts attributable to the parent's owners and the non-controlling interest component; and
- any difference between the consideration paid or received and the amount by which non-controlling interests are adjusted is recognised in equity (not in OCI), and attributed to owners of the parent (IAS 27.31).

As noted above, Grant Thornton believes that 'reallocation' is required in respect of all components of equity that relate to cumulative OCI. IAS 21.48C is explicit that this reallocation is required on a decrease in ownership interest (partial disposal) of a subsidiary that includes a foreign operation. IFRS does not provide explicit guidance on reallocation of other components of equity. In Grant Thornton’s view reallocation is the most appropriate treatment in relation to revaluation reserves, AFS reserves etc (both on an increase and a decrease in ownership). This is because reallocation results in each component of equity attributable to the controlling interest displaying the proportion of the applicable gain or loss to which the parent's owners would be entitled on realisation. We also believe this approach is consistent with IAS 27.31.

Example 3: Change in ownership interest

Entity P owns 100% of Entity S (a foreign operation) which was acquired in a previous business combination. The consideration transferred at the acquisition date was $3,000. At 31 March 20X1 Entity S's net assets (as reported in Entity P's consolidated financial statements) are $5,000. The consolidated financial statements also include the following components of equity relating to S: retained earnings of $1,000; revaluation surplus of $1,200 and foreign currency translation reserve of $(200). On 31 March 20X1 Entity P sells 20% of its shares in S to an unrelated third party investor for cash of $1,100. Transaction costs are insignificant. The accounting entries recorded in the consolidated financial statements are:

	Dr	**Cr**
Cash	1,100	
Non-controlling interests (equity) (note 1)		1,000
Revaluation surplus (equity)	240	
Currency translation reserve (equity)		40
Retained earnings (equity) (note 2)		300

Notes:

1. The change in non-controlling interests is 20% of Entity S's net assets ie $1,000. This represents: reallocation of the revaluation surplus and currency translation reserve $200 [20%*(1,200 - 200)]; and recognition of the proportionate share of the non-controlling interests' share of other equity of $800 [20%*(5,000 - 1,200 + 200)].

2. The increase in retained earnings of $300 can be rationalised as the notional 'gain' on the part disposal of $100 [1,100 - (20%*$5,000)] plus the 'realisation' of 20% of the revaluation surplus

and currency translation reserve.

In this example Entity P owns 100% of Entity S prior to the transaction in question (ie there is no non-controlling interest). If there are pre-existing non-controlling interests that were measured at fair value (as permitted by IFRS 3(2008).19), the total of non-controlling interests will not normally equal the proportionate interest in the subsidiary's recognised net assets. There may also be other factors affecting the recognised amount of non-controlling interests eg the existence of different classes of equity.

OCI and loss of control of subsidiary

The requirements on loss of control of subsidiaries are set out in IAS 27.32 - 37. The parent entity recognises a gain or loss on when it loses control. This gain or loss is attributed to the parent's owners. It is determined as the difference after the parent (IAS 27.34):

- derecognises the assets and liabilities of the subsidiary (including goodwill);
- derecognises the non-controlling interest including any attributable components of OCI;
- recognises:
  - the fair value of the consideration received (if any)
  - if applicable, the distribution of shares in the subsidiary to owners (in their capacity as owners);
  - the fair value of any investment retained in the former subsidiary;
- accounts for any amounts recorded in OCI in the same way as they would be treated if the related assets and liabilities had been disposed of directly (IAS 27.35).

In applying this final requirement, it should be noted that IAS 21.48B sets out more specific requirements on how to deal with the currency translation reserve. It states that:

> 'On disposal of a subsidiary that includes a foreign operation, the cumulative amount of the exchange differences relating to that foreign operation that have been attributed to the non-controlling interests shall be derecognised, but shall not be reclassified to profit or loss.'

In other words, only the parent's share of the currency translation reserve is reclassified to profit or loss. For other items of comprehensive income for which reclassification adjustments are required by IFRS (available-for-sale assets and cash flow hedging reserves), in Grant Thornton's view the entire gain or loss should be reclassified. This approach is consistent with the accounting when the related assets or liabilities are disposed of directly and is therefore consistent with IAS 27.35. This approach affects the allocation of the total gain or loss among its components, but does not affect the net amount of gain or loss.

Example 4: Loss of control

Entity P owns 75% of Entity S (which includes a foreign operation). At 30 September 20X1 the amounts included in Entity P's consolidated financial statements relating to Entity S are as follows:

	Note	$
Available for sale (AFS) asset	1	1,200
Revalued property	2	2,000
Other assets and liabilities		800
Net assets		4,000

Equally attributable to the parent:

Accumulated OCI	**Note**	**$**
AFS Reserve	3	150
Currency translation reserve	3	75
Revaluation surplus	3	300
Other reserves	4	2,475
Non-controlling interests	5	1,000
Total equity		4,000

Notes

1. Comprising cost $1,000 and recognised fair value increase $200
2. Including revaluation surplus $400
3. Net of amounts attributed to non-controlling interests
4. P's share of equity on acquisition $1,500 plus post acquisition retained earnings $975
5. NCI's share of: Entity S's equity at acquisition $500; post acquisition retained earnings $325; accumulated OCI $175

On 30 September 20X1 Entity P disposes of its entire interest in Entity S for cash consideration of $3,600. How is the disposal accounted for?

The accounting entries recorded in the consolidated financial statements are:

	Dr	Cr
Cash	3,600	
Net assets of S		4,000
Gain on disposal of AFS asset (P&L) (note 1)		200
AFS reserve	150	
Currency gain (P&L) (note 2)		75
Currency translation reserve (equity)	75	
Revaluation surplus (note 3)	300	
Retained earnings (equity)		300
Non-controlling interests	1,000	
Gain on disposal of S (P&L) (note 4)		550

Notes

- The entire fair value increase relating to the AFS assets is reclassified to profit or loss, including the amount attributable to non-controlling interests. This is because the entire amount would have been reclassified if the AFS assets had been disposed of directly (IAS 27.35).

- By contrast, with the currency translation reserve only the amount attributable to the parent's owners is reclassified in accordance with IAS 21.48B.

- It is common practice for entities that apply IAS 16's revaluation model to reclassify the revaluation surplus to retained earnings on disposal (as a reserve transfer within equity not into profit or loss). A reclassification within equity is permitted but not required (IAS 16.41). If an entity adopts this accounting policy on a direct disposal of revalued property, the same reclassification is made on loss of control of a subsidiary in order to comply with IAS 27.35.

The gain on disposal is the balancing item as determined in accordance with IAS 27.34. Intuitively, the gain might be expected to be $600 (proceeds of $3,600 less 75% of $4,000). However, the effect of recognising the entire fair value increase relating to the AFS assets is to restrict the gain on disposal of S by $50 (the amount of the AFS gain attributable to the non-controlling interests). The transaction gives rise to an overall gain of $825 (550+200+75). This gain can be rationalised as: the 'expected' gain of $600 plus the parent's share of the cumulative OCI items that are reclassified to profit or loss (the AFS and currency translation reserves).

OCI and equity accounting

This alert provides guidance on accounting for OCI that relates to a subsidiary in which there is a non-controlling interest. It is not intended to provide detailed guidance on OCI that arises in the financial statements of equity accounted investments (ie most associates and also jointly controlled entities when the investor elects to apply the equity method). In summary, however, it should be noted that:

- the investor recognises its share of OCI of the associate (or jointly controlled entity) within its own OCI (IAS 28.11)
- reclassification adjustments are made on loss of significant influence (or loss of joint control) in a similar manner to loss of control of a subsidiary (ie if direct disposal of the related assets or liabilities would result in a reclassification adjustment) (IAS 28.19A)
- if the investor reduces its interest in the associate without a loss of significant influence, a proportionate reclassification adjustment is recorded (IAS 28.19A). This accounting treatment therefore differs from the treatment of OCI on a change in ownership interest of a subsidiary.

Note
On 12 November 2009, the IASB published IFRS 9 *Financial Instruments* (IFRS 9). IFRS 9 addresses the classification and measurement of financial assets. The publication of IFRS 9 represents the completion of Phase 1 of IASB's project to replace IAS 39. However, at this stage IFRS 9 only addresses the classification and measurement of financial assets. Financial liabilities therefore continue to be accounted for in accordance with IAS 39. Work has begun on Phases 2 and 3 of the project which addresses impairment and hedge accounting, respectively. Also, a separate project is underway to replace IAS 39's requirements on derecognition. IFRS 9 was issued in Australia as AASB 9 Financial Instruments with an effective date of 1 January 2013 and therefore AASB 9 requirements have not been considered for the purpose of this alert.

Further information

For further information on any of the information included in this TA alert, please contact your local Grant Thornton Australia contact member or a member of the National Audit Support team via the GTAL IT Service Desk http://gtassist.au.gt.local/