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Fact Sheet FS 029 | 10 March 2023

AASB 10 Consolidated Financial Statements

This standard establishes the principles for the presentation and preparation of consolidated financial statements when an entity (investor) controls one or more other entities (investees).

Appendix E to AASB 10 provides guidance for not-for-profit entities in applying the standard.

This standard requires an entity (the parent) that controls one or more other entities (subsidiaries) to present consolidated financial statements. Therefore, a reporting unit that controls one or more subsidiaries is required to prepare consolidated financial statements in accordance with AASB 10 from the date it obtains **control** of the investee.

The assessment of whether a reporting unit has control is judgemental and requires a reporting unit to collate facts surrounding the relationship in order to make a balanced assessment.

What determines 'control' of an investee?

Control assessment

A reporting unit will control an investee where it has:

- power over the investee;
- exposure or rights to variable returns from its involvement with the investee; and
- ability to use its power over the investee to affect the amount of the reporting unit's return.

A reporting unit should consider the purpose and design of the investee to identify the relevant activities, how decisions about the relevant activities are made, who has the current ability to direct those activities and who receives returns from those activities.

The main steps and considerations for a reporting unit when assessing control can be summarised as follows:

1. Identifying relevant activities

Identify which activities of the investee are considered the ‘relevant activities’, i.e. those activities of the investee that affect the investee’s return.

Examples of relevant activities include:

- establishing operating, capital and financing policies
- selling and purchasing goods and services
- acquiring and disposing of assets
- obtaining funding
- appointing, remunerating and terminating employment of service providers or key management personnel
- setting policy directions

2. Evaluating power

Determine which party, if any, has power, that is, the current ability to direct those activities. Power arises from those rights, which may include:

- voting rights
- rights to appoint and remove key management or board personnel
- contractual rights
- rights arising from statutory/legislative arrangements
- rights to give policy directions to the governing body
- rights to approve/veto capital and operational budgets

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3. Assessing returns

Assess whether the investor is exposed, or has rights, to variable returns from its involvement with the investee. Returns can be financial, non-financial, direct or indirect benefits, whether positive or negative.

Examples of returns include:

- achievement or furtherance of investor's social objectives
- dividends, returns, net assets
- remuneration
- returns that are not available to other interest holders (e.g. economies of scale, cost savings)

Considerations when making an assessment on control

Reporting units should consider the following:

Factors	Discussion
Does the reporting unit hold a majority of the voting rights?	Voting rights by themselves do not give rise to power, however, if the reporting unit has: • the majority of the voting rights, or • the ability to appoint directors with the power to cast a deciding vote or veto decisions then the reporting unit may have power to direct the relevant activities of the investee. However, in some cases, voting rights may relate to administrative tasks only. Therefore, it may be necessary to consider other factors even if the reporting unit holds the majority of the voting rights.

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Factors	Discussion
Are the investee's directors / key management personnel (KMP) current or previous employees of the reporting unit or have the directors / KMP been appointed by the reporting unit?	Similar directors/KMP do not necessarily give rise to power in itself however, if: • the majority of the investee's directors/KMP are similar/same as the reporting unit, or current/former employees of the reporting unit; or • the investee's directors/KMP are appointed by the reporting unit; or • the investee's directors/KMP who have been appointed by the reporting unit have the ability to independently direct the operating/decision making activities of the entity; then the reporting unit may have the power to direct the relevant activities of the investee.
Does the investee rely on the reporting unit for continued support?	If the reporting unit funds a significant portion of the investees' operations or provides guarantees for the investee's obligations, then the reporting unit is likely to be involved in the budgeting process of the investee or the operating decisions affecting returns/repayment of funds. Financial dependence in the absence of other rights, does not necessarily lead to power, however, continuing support/guarantees along with the associated rights may indicate the reporting unit has power over the investee.

Factors	Discussion
Are the activities of the investee conducted on behalf of the reporting unit (or for the reporting unit's benefit)?	If it appears the reporting unit established the investee for conducting its own activities or solely for its own benefit, the reporting unit may have retained rights to apply power over the investee.
Is the reporting unit's exposure to returns from the investee equivalent to the reporting unit's voting or other similar rights?	If the reporting unit's exposure, or rights, to returns from its involvement with the investee is greater than its voting or other similar rights, this could indicate other factors/rights are present which may give rise to power. The greater the exposure to variable returns, the greater the incentive to retain power over the investee.

How do I prepare consolidated financial statements?

In summary, the procedures required to prepare consolidated financial statements are as follows:

- combine like items of assets, liabilities, equity, income, expenses and cash flows of the parent with those of its subsidiaries
- offset (eliminate) the carrying amount of the parent's investment in each subsidiary and the parent's portion of equity of each subsidiary
- eliminate in full intragroup assets and liabilities, equity, income, expenses and cash flows relating to transactions between entities of the group

AASB 10 requires that the parent and the subsidiaries use uniform accounting policies for like transactions.

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So what does a reporting unit need to consider?

1. In assessing power, only substantive rights relating to the investee are considered. A right will be substantive where the reporting unit has the practical ability to exercise the right, therefore when making an assessment on whether rights are substantive a reporting unit should consider if there are any barriers to exercising their rights.

2. A reporting unit with decision-making rights within an investee must determine whether it is a **principal** acting in its own right, or an **agent** with delegated power. An agent is primarily engaged to make decisions on behalf of a principal. As such, the powers held by the agent are attributed to the principal when determining the existence of control. A reporting unit acting as a principal may control an investee, whilst a reporting unit acting solely as an agent cannot control an investee.

   Example

   A reporting unit establishes a trust to fund a particular objective and appoints the trustee. The reporting unit must assess whether it controls the trust through the trustee. If the trustee has the power to affect the day-to-day operating decisions which impact the returns of the trust, but the reporting unit can replace the trustee at its discretion, then it is likely the trustee is acting as an agent and it is the reporting unit which controls the trust.

3. AASB 12 Disclosure of Interests in Other Entities includes all the disclosure requirements for subsidiaries, joint arrangements, associates and consolidated and unconsolidated structured entities.

   The recognition and measurement of subsidiaries, joint arrangements and associates are dealt with in AASB 10, AASB 11 Joint Arrangements, AASB 127 Separate financial statements and AASB 128 Investments in Associates and Joint Ventures.