Ihre Ansprechpartner

Sehr geehrte Damen und Herren,

für Rückfragen zu der beigefügten Publikation „In brief“ zur Thematik
“Consolidation considerations for Venezuelan subsidiaries”
stehen Ihnen folgende Ansprechpartner gerne zur Verfügung:

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In brief

A look at current financial reporting issues

20 January 2015

Consolidation considerations for Venezuelan subsidiaries

Issue

Venezuela is a hyperinflationary economy and the government maintains a regime of strict currency controls. Multinational companies are facing significant difficulty in repatriating earnings from Venezuelan subsidiaries. There is significant uncertainty about exchange rates available, the amount that can be repatriated at a given exchange rate and the timing of repatriation. There is some speculation that the current exchange rate mechanisms may change. There is a continuing high level of government regulation (that is, fair price regulation and labour law) that might impose limitations on the decision-making powers of management.

In December 2014, a registrant precleared with the SEC staff the registrant's conclusion to deconsolidate its Venezuelan operations and begin accounting for such operations as a cost method investment under US GAAP. (See US In-brief No.US 2015-2).

Some have questioned whether continuing uncertainty and difficulty in repatriation mean that multinational companies should consider de-consolidation of their Venezuelan subsidiaries under IFRS.

Impact

Multinational companies should only de-consolidate Venezuelan subsidiaries if they no longer meet the three criteria for control under IFRS 10. Uncertainty about repatriation of profits and current exchange difficulties alone are unlikely to result in a loss of control under IFRS 10. However, each circumstance should be addressed on its individual merits.

An investor controls an investee if it has all of the following elements (IFRS 10 para 7 (a)(c)):

1) power over the investee;
2) exposure , or rights, to variable returns from its involvement with the investee; and
3) the ability to use its power over the investee to affect the amount of the investor's returns.

If one or more of the elements of control changes an entity should reassess control.

An investor will lose control of its subsidiary when it no longer has the power to direct its relevant activities and hence loses the ability to vary its returns. This is a high hurdle. Where an entity has power, it must demonstrate that it has no exposure to variable returns to determine it does not have control. Difficulty in repatriating earnings, and uncertainty about the exchange rate, is not the same as a loss of control.

This follows from paragraph B83 of IFRS 10 that states "*An investor that has power over an investee can lose control of an investee if the investor ceases to be entitled to receive returns or to be exposed to obligations.*"

A parent that continues to direct the relevant activities of its investee in Venezuela meets the power criterion. It is likely to remain exposed to the variable returns. Those returns could be positive or negative and are not only financial in nature (see IFRS 10 paras B56 and B57).

A full assessment of control should be performed and include the following:

- the parent's permanent inability to repatriate any profits or benefits from its Venezuelan operation;
- the impact of government regulations on the ability to make decisions relating to all relevant activities of the Venezuelan operation, for example capital structure, product pricing and labour relations; and
- the political and economic situation within Venezuela, including expropriation of all assets of the Venezuelan operation.

Different multinational parents may find themselves in different circumstances. Each fact pattern should be carefully considered, however, we believe that most multinational parents with subsidiaries in Venezuela will continue to consolidate in the current environment.

Previous exceptions to consolidation

A much earlier version of the consolidation guidance under IFRS (IAS 27, revised in 2003 as part of the first 'Improvements') contained a number of exceptions to consolidation including 'foreign exchange restrictions, controls, or other governmentally imposed uncertainties so severe that they cast significant doubt on the parent's ability to control the subsidiary.'

This specific exception has been removed from IFRS; however, it does remain as a consideration under US GAAP. A parent needs to consider whether that significant doubt about control exists. An entity should also consider the level of disclosure required to meet the requirement to disclose significant judgements and assumptions made in its control assessment. [IFRS 12 para 7]. An entity is also required to disclose significant restrictions on its ability to access or use the assets and settle the liabilities of the group. [IFRS 12 para 13].

Related topics

See related In brief INT2014-16 for our most recent guidance on Venezuela and exchange rates. Further changes to the foreign exchange market in Venezuela may occur.