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Reported revenues could fall under new IFRS rules

by Richard Crump 24 Jan 2014

NEW REPORTING STANDARDS which update the rules on group accounting will result in a material fall in reported revenues, assets and liabilities for some European corporates, Fitch Ratings has said.

The rules, which were introduced in 2013, will affect how companies account for, and disclose, their interests in subsidiaries, joint arrangements, associates and unconsolidated structured entities

"In some cases, these changes will have a significant effect on key financial statement metrics, including revenue, EBIT, cash flow, gross assets and debt," the rating agency said.

IFRS 10 contains new consolidation rules, which may affect the number of subsidiaries included in the group accounts, while IFRS 11 prescribes new accounting rules for joint arrangements.

Significantly, IFRS 11 *Joint Arrangements* prescribes new accounting rules that prohibit proportionate consolidation for what are now defined as 'joint ventures.' For structures that are classified as 'joint operations,' a method similar to proportionate consolidation is now required.

The Fitch survey, of 24 large European non-financial corporates, found 13 of these entities had been using proportionate consolidation to account for interests in jointly controlled entities. IFRS 11 will force companies to use equity accounting instead for structures that are classified as 'joint ventures.'

The three companies most greatly affected - Vodafone Group, Robert Bosch and BASF- see revenue reductions of €7.6bn (£6.2bn), €7.3bn and €6.6bn respectively.

"The changes have the potential to affect any line in the financial statements. Moving from proportionate consolidation to the equity method will reduce revenue and expenses, gross assets, and liabilities, which will be particularly significant if debt sits in the joint venture," the report said.

"However, profitability might increase if the joint venture is loss-making, as the equity method may restrict recognition of losses."

Fitch's survey also found that IFRS 10 *Consolidated Financial Statements* will not have a significant affect for most companies.

"The changes introduced by the standard were targeted in particular at off-balance sheet structured entities and most of the group relationships that non-financial corporates have will be unaffected by the new rules," it said.