



Solution 20.4

Component	Control, joint control and significant influence
Index	What is control?
Short title	Control via power to govern the financial or operating policies by agreement or statute

Attention: This guidance is based on the revised standards and interpretations that are mandatory for accounting periods commencing 1 January 2005.

Issue

There is a presumption that the acquisition of more than one half of another entity's voting rights confers control [IAS27.13 (R.05)]. However, factors other than ownership can also hand control to a parent that does not own more than half the voting rights.

How would power to govern an entity's financial or operating policies lead to control?

Background

Three entities, A, B and C invest in a fourth, D, to manufacture footballs. Entity A has considerable experience of manufacturing footballs and has developed new technology to improve the production processes and the footballs' performance. Entities B and C are both banks which have previously financed A's operations.

Entity A will contribute technology and know-how to D, while B and C will contribute finance. The share ownership will be A: 40%, B: 30% and C: 30%. Each entity will appoint directors in proportion to their ownership percentage. An agreement between the shareholders states that all directors will be non-executive except for the managing director and the finance director, both of whom A will appoint in recognition of its expertise in the area of football manufacture.

The shareholder agreement delegates the power to set D's operating policies and budget to the managing director and the finance director; however, the full board must consider requests for additional financing.

Solution

Delegating powers over the entity's operating policies and budget to the directors that A appointed, provides A with effective control over D. Although the full board retains some powers, including decisions about changes to financing and share structure, these are limited and provide rights that are more protective than participative.



The decisions concerning financial and operating policies represent a substantial part of the total range of decisions to be taken in respect of the operating entity. Control over the financial and operating decisions therefore provides substantial control over the entity.