Solution 20.5

Component	Control, joint control and significant influence
Index	What is control?
Short title	Control via right to appoint the majority of the board

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 which does not own more than half the voting rights.

How can an entity's ability to appoint or remove the majority of the board of directors confer control?

Background

Entity A owns 45% of the shares in entity X but, based on the shareholders agreement, controls the composition of the board of directors, with the power to appoint and remove the majority of them.

Amendments to X's articles of incorporation state that acquisitions and disposals of assets in an amount higher than 50% percent of the fair value of X's total assets, and the decision to liquidate X, are reserved for shareholder vote.

Solution

Certain decisions are reserved for shareholder vote and are protective in nature. Provided the decisions reserved for shareholder vote do not interfere with the operations of entity X, entity A will be able to control X's financial and operating policies so as to obtain benefits from its activities.

Difficulties may arise in judging whether the power to appoint or remove most of the board confers control. Certain entities in some countries are required to have a supervisory board and a management board. Power relating to either board should be considered. The supervisory board generally appoints the management board, so it is power over the supervisory board that is relevant.

The board of directors exercises effective control of the entity, therefore the ability to control the board's composition confers control.

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