

**AMENDMENT TO FRS**

**AMENDMENT TO FRS 2**

**‘ACCOUNTING FOR SUBSIDIARY UNDERTAKINGS’**

**LEGAL CHANGES**



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*“Amendment to Financial Reporting Standard 2  
Accounting for Subsidiary Undertakings: Legal  
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Institute of Chartered Accountants in Ireland in  
respect of its application in the Republic of Ireland.*

**AMENDMENT TO FRS 2**

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## **PREFACE**

1. This Amendment to FRS 2, 'Accounting for Subsidiary Undertakings', reflects certain changes to the law introduced by the Companies Act 1985 (International Accounting Standards and Other Accounting Amendments) Regulations 2004.
2. In March 2004 the Department of Trade and Industry (DTI) issued a Consultation Document, 'Modernisation of Accounting Directives/IAS Infrastructure'. In response to the proposed legal changes an Exposure Draft, 'Accounting for Subsidiary Undertakings – Legal Changes', was issued in May 2004. The Exposure Draft was based on the proposals set out in the Consultation Document.
3. Respondents to the Exposure Draft generally agreed with its proposals. Changes from the Exposure Draft reflect only changes to the draft Regulations. The most significant of these is the amendment to section 258(4) in the definition of parent and subsidiary undertakings to include 'it has the power to exercise, or actually exercises, dominant influence or control over it'.
4. These changes extend the definition of a subsidiary undertaking. As a result, some entities previously accounted for as 'quasi-subsidiaries,' in accordance with FRS 5 'Reporting the Substance of Transactions,' may now meet the definition of a subsidiary undertaking within the meaning of the Companies Act and this Standard.
5. Some respondents questioned whether the removal of 'participating interest' from the definition of a subsidiary undertaking in paragraph 14(e) introduced ambiguity, as the actual exercise of dominant influence might be thought to be sufficient to require consolidation even where there is no benefit to the holder. However, the

definition in paragraph 7(b) of ‘the actual exercise of dominant influence’ requires influence that achieves operating and financial policies set in accordance with the holder’s wishes and for its benefit. Accordingly there seems no doubt that an entity should only be consolidated on grounds of ‘actual exercise of dominant influence’ where the parent undertaking receives the benefits.

6. The FRS has also been amended to clarify that ‘power to exercise dominant influence’ is to be interpreted as a power that, if exercised, would give rise to the actual exercise of dominant influence as defined in paragraph 7(b). Accordingly an undertaking will be a subsidiary on these grounds only where the parent undertaking has the potential to receive benefit.
7. The Regulations also permit an interest held exclusively with a view to subsequent resale to be excluded from consolidation, irrespective of whether or not it has been previously included in the consolidated financial statements of the parent undertaking. As explained in the Exposure Draft, the ASB believes that where a subsidiary has been previously reported as part of the continuing operations of the group, it should only cease to be reported as part of the continuing operations when the subsidiary undertaking is sold (or terminated) and meets the definition of a discontinued operation\*. Respondents generally agreed with the proposal, set out in the Exposure Draft, not to amend the FRS in this respect.
8. In summary the amendments to FRS 2:
  - a. reflect the changes in the law, deleting references to ‘participating interest’ in the definition of a subsidiary

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\* *Discontinued operations are defined in FRS 3 ‘Reporting Financial Performance’.*

undertaking and introducing ‘the power to exercise or actually exercise, dominant influence or control’;

- b. reflect the exemption from the preparation of consolidated accounts for intermediate parent undertakings whose immediate parents are not governed by the law of an European Economic Area (EEA) State; and
- c. remove the requirement for exclusion from consolidation of subsidiaries with dissimilar operations to the parent undertaking.



## **STATEMENT OF STANDARD ACCOUNTING PRACTICE**

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### ***Amendment to FRS 2 ‘Accounting for Subsidiary Undertakings – Legal Changes’***

1. Paragraph e(iii) is renumbered e(iv).
2. New paragraph e(iii) is inserted as follows:

“it is a wholly-owned or majority-owned subsidiary undertaking and its parent undertaking is not established under the law of an EEA State. Exemption is conditional on compliance with certain further conditions in section 228A; or”
3. Insert in the margin alongside paragraph 6:

*[FRS defining phase used in s258(4)(a)]*
4. New Paragraph 7c is inserted as follows:
  - c *The power to exercise dominant influence* is a power that, if exercised, would give rise to the actual exercise of dominant influence as defined in paragraph 7b.
5. Paragraph 14e is replaced with the following:
  - i it has the power to exercise, or actually exercises, dominant influence or control over the undertaking;  
or
  - ii it and the undertaking are managed on a unified basis.
6. Paragraph 19A is renumbered 19B.
7. Paragraph 19A is inserted as follows:

“This Standard does not apply to retirement benefit

schemes, which are within the scope of FRS 17 'Retirement benefits'."

8. Paragraph 21a is amended as follows:

"The group is small or medium-sized and is not an ineligible group as defined in section 248. A group is ineligible if any of its members is a public company, ~~a banking institution, an insurance company or an authorised person under the Financial Services Act 1986~~ a person who carries on an insurance market activity or a person who has permission under Part 4 of the Financial Services and Markets Act 2000 to carry on a regulated activity."

9. Paragraph 21b is amended as follow:

"The parent undertaking is a wholly-owned subsidiary undertaking and its immediate parent undertaking is established under the law ~~of a member state of the European Community~~ an EEA State. Exemption is conditional on compliance with certain further conditions set out in section 228(2). A parent undertaking is not exempt if any of its securities ~~is listed on a stock exchange in any European Community country~~ are admitted to trading on a regulated market of any EEA State within the meaning of Council Directive 93/22/EEC."

10. Paragraph 21d is renumbered 21f.

11. New paragraph 21d is inserted as follows:

"The parent undertaking is a wholly owned subsidiary of another undertaking and that parent undertaking is not established under the law of an EEA State. Exemption is conditional on compliance with certain further conditions set out in section 228A(2). The exemption [228A] does not apply to a parent undertaking if any of its securities are admitted to trading on a regulated market

of any EEA State within the meaning of Council Directive 93/22/EEC.”

12. New paragraph 21e is inserted as follows:

“The parent undertaking is a majority-owned subsidiary undertaking and meets all of the conditions for exemption as a wholly owned subsidiary undertaking set out in section 228A(2) as well as the additional conditions set out in section 228A(1)(b).”

13. Paragraph 25 is amended by the deletion of "... and (4)" from the first sentence. The reference in the margin alongside paragraph 25 is amended by the deletion of "... and (4)".

14. Amend the reference in the margin alongside paragraph 25b to say:

*“[FRS restricts exclusion permitted by s229(3)(c)]”*

15. Paragraph 34 is replaced with:

“Where an undertaking is a subsidiary undertaking only because its parent undertaking has the power to exercise, or actually exercises, dominant influence or control over it, the consolidated financial statements should disclose the basis of the parent undertaking’s dominant influence or control in addition to the disclosures required, subject to section 231, by Schedule 5 paragraph 15(5).”

16. Paragraph 39 is amended by the deletion of the final sentence.

17. Delete the reference in the margin alongside paragraph 44.

18. Paragraphs 57 and 58 are deleted and replaced by the following:

“Compliance with the amended FRS ensures substantial compliance with the relevant provisions of International Accounting Standard 27 ‘Consolidated and Separate Financial Statements’ (IAS 27), as amended by IFRS 5 ‘Non-current Assets Held for Sale and Discontinued Operations’. However, IAS 27: (a) does not include an exemption from consolidation for subsidiaries where severe long-term restrictions exist and (b) does not exempt subsidiaries that are held exclusively with a view to resale. IFRS 5 requires newly acquired subsidiaries held for sale to be measured at the lower of carrying value and fair value less costs to sell; the assets and liabilities of the subsidiary may not be offset and should be presented separately from other assets and liabilities in the balance sheet\*.”

19. Paragraph 62 is amended as follows:

“The accounting concept that underlies the presentation of consolidated financial statements for a group as a single economic entity is summarised in the definition of control in paragraph 6. Although the definition of parent and subsidiary undertakings in the Act are founded mainly on the accounting concept of control, section 258 uses a list of tests ~~including rather than relying on control directly~~ to determine which undertakings are parent and subsidiary undertakings. In the main the effect of applying the tests in the Act is same as using a criterion based ~~solely directly~~ on the accounting concept of control. ~~However, in some cases the test of the Act may either fail to identify as a subsidiary undertaking one that is controlled by another undertaking or identify as a subsidiary undertaking one that is not controlled by its parent undertaking. In other~~ There may, however, be cases where section 258 ~~may identify~~ identifies more than one undertaking as the parent undertaking of the

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\* The assets and liabilities of the newly acquired subsidiary held for sale may be presented together with the assets and liabilities of any other assets or disposal groups held for sale by the entity.

same subsidiary undertaking. Where more than one undertaking is thereby identified as a parent of one subsidiary undertaking, not more than one of those parents can have control as defined in paragraph 6.”

20. Paragraph 71 is amended as follows:

“In a second reference to dominant influence, section 258(4)(a) identifies an undertaking as the subsidiary undertaking of another (its parent undertaking) if that other ~~has a participating interest in it and actually exercises a dominant influence~~ the power to exercise, or actually exercises, dominant influence over it. Schedule 10A paragraph 4(3) provides that the definition of the ‘right to exercise a dominant influence’ for the purposes of section 258(2)(c) shall not affect the construction of ‘actually exercises a dominant influence’ in section 258(4)(a). The FRS defines the ‘actual exercise of dominant influence’ as the exercise of an influence that achieves the result that the operating and financial policies of the undertaking influenced are set in accordance with the wishes of the holder of the influence and for its benefit (whether or not those wishes are explicit). The FRS defines ‘the power to exercise dominant influence’ as a power that, if exercised, would give rise to the actual exercise of dominant influence.”

21. Paragraph 74 is amended as follows:

“... if it ~~has a participating interest in~~ and that other undertaking ~~and they~~ are managed on a unified basis.”

22. Paragraph 76 is amended as follows:

“The Act requires that all the subsidiary undertakings of a parent undertaking are to be included in the consolidated financial statements for that group, subject to the exemptions permitted ~~or required~~ by section 229(2) and ~~(34)~~. The circumstances in which the Act

permits ~~or requires~~ a subsidiary undertaking to be excluded from consolidation are the following:

~~Permissive exclusions~~

...

- d 'where the interest of the parent company is held exclusively with a view to subsequent resale ~~and the undertaking has not previously been included in consolidated group accounts prepared by the parent company~~';

...”

Sub-paragraph e and its heading are deleted.

23. Paragraph 78 is amended as follows:

“In order to help preparers identify the exceptional circumstances where it is inappropriate to consolidate a subsidiary undertaking, the exclusions allowed ~~or required~~ by section 229(2) and ~~(34)~~ are discussed below.

...”

Sub-paragraph e and its heading are deleted.

24. In paragraph 83 delete the sentence that starts “Where there are subsidiary undertakings excluded from consolidation because of their different activities ...”.

25. In paragraph 95 insert, where appropriate:

Section 228A ‘Exemption for parent companies included in non-EEA group accounts’

26. In paragraph 95 delete reference to Section 260.

27. The following paragraphs are deleted:

g(iii), h(iii), 15, 25c, 30, 31d, 79c

28. Paragraph 98 is amended as follows:

*References in text:*

Paragraph a	Amend Republic of Ireland reference to	The Companies Acts 1963 – 2003 and the European Communities (Companies: Group Accounts) Regulations 1992 (“the Regulations”)
Paragraph 21b	Amend Republic of Ireland reference to	Regulation 8(3)
Paragraph 21c	Amend Republic of Ireland reference to	Regulation 8(1)(b)
Paragraph 35	Amend Republic of Ireland reference to	Regulation Schedule para 8(2)
Paragraph 36 Schedule 4A 17(3)	Amend Republic of Ireland reference to	Regulation Schedule para’s 9(1) – (2)
Paragraph 36 Schedule 4A 17(4)	Amend Republic of Ireland reference to	Regulation Schedule para’s 9(3) – (4)
Paragraph 41	Amend Republic of Ireland reference to	Regulations 29(3) and 30(3)
Paragraph 45	Amend Republic of Ireland reference to	Regulation 19 does not mention the date of acquisition.
Paragraph 50	Amend Republic of Ireland reference to	Regulation 19(2)

*References in explanation:*

Paragraph 71 Section 258(2)(c)	Amend Republic of Ireland reference to	Regulation 4(1)(b)
Paragraph 88	Amend GB reference	Schedule 4A para 9
Paragraph 88	Amend Republic of Ireland reference to	Regulation 19

*References in margins:*

Paragraph 10	Amend Republic of Ireland reference to	Regulation 35(1)
Paragraph 14c(i)	Insert Republic of Ireland reference to	Regulation 4(1)(b)(i)
Paragraph 20	Amend Republic of Ireland reference to	Regulation 5 (1), 7,8,9,10-12
Paragraph 21a	Amend Republic of Ireland reference to	Regulation 6&7
Paragraph 21d	Amend Republic of Ireland reference to	No Irish equivalent to 229(5)
Paragraph 22	Insert Republic of Ireland reference to	Regulation 8(3)(d)
Paragraph 30	Amend Republic of Ireland reference to	Companies (Amendment)Act 1986 section 16
Paragraph 35	Amend Republic of Ireland reference to	Regulation Schedule para 8(2)
Paragraph 36	Amend Republic of Ireland reference to	Regulation Schedule para 9
Paragraph 41	Insert Republic of Ireland reference to	Regulations 29(3) and 30(3)
Paragraph 48	Insert Republic of Ireland reference to	No Irish equivalent
Paragraph 46	Delete from table	

29. The following should be added to the foot of ‘The development of the Standard’:

**Amendment to FRS 2: Legal Changes**

xxv In 2004 FRS 2 was amended to reflect changes to the Act that were introduced by the Companies Act 1985 (International Accounting Standards and Other Accounting Amendments) Regulations 2004 (SI 2004 No. 2947).

**Date from which effective**

This amendment takes effect for accounting periods beginning on or after 1 January 2005.

**ADOPTION OF AMENDMENT TO FRS 2  
BY THE ACCOUNTING STANDARDS  
BOARD**

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“Amendment to Financial Reporting Standard 2 ‘Accounting for Subsidiary Undertakings’: Legal Changes” was approved for issue by the ten members of the Accounting Standards Board.

Ian Mackintosh	Chairman
Andrew Lennard	Technical Director
Michael Ashley	
Douglas Flint	
Anthony Good	
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