Disclosure of Non-Controlling Interests

Supervision of Financial Reporting

October 2012

Contents

The Netherlands Authority for the Financial Markets

The AFM promotes fair and transparent financial markets. We are the independent supervisory authority for the savings, lending, investment and insurance markets. The AFM promotes the conscientious provision of financial services to consumers and supervises the honest and efficient operation of the capital markets. Our aim is to improve consumers' and the business sector's confidence in the financial markets, both in the Netherlands and abroad. In performing this task the AFM contributes to the prosperity and economic reputation of the Netherlands.

1 Executive Summary

The thematic review is conducted in anticipation of the new standard requiring disclosure of non-controlling interests (IFRS 12) that is expected to apply in the European Union on 1 January 2014.

In this report, a non-controlling interest is defined as a consolidated (group) company in which the parent has an interest of less than 100% (and therefore another company has a non-controlling interest in group equity).

Based on the thematic review it conducted of non-controlling interests, the AFM has observed the following:

- **25% to 50% of the companies have a material (or potentially material) non-controlling interest;**
- **Companies are not yet providing transparency regarding the effect of non-controlling interests on the financial position, financial results and cash flows of the group;**
- **14 (of the 42) companies do not provide a proper description of the composition of the group.**

The AFM urges companies to include an up-to-date list of ownership interests in their financial statements or in the Trade Register, in order to meet the need of investors for the information they require to gain a good understanding of the composition of the group and the (potential) effect of this on the group's financial position, financial results and cash flows.

25% to 50% of the companies have a material (or potentially material) non-controlling interest
The interests of third parties in one or more group companies (non-controlling interests) form a material part of the total group equity of a quarter of the companies subject to supervision. For a further quarter of the companies under supervision, the size of these interests measured as part of total group equity is not material. This, however, does not exclude the possibility that these non-controlling interests may well have a material effect on one or more individual items in the financial statements. The fact that 25% to 50% of the companies subject to supervision have a material or potentially material non-controlling interest means that transparency regarding the effect of non-controlling interests on the financial position, financial results and cash flows, and thereby the risks of the group, is important to investors.

Companies are not yet providing transparency regarding the effect of non-controlling interests on the financial position, financial results and cash flows of the group
The AFM observes that companies are not yet providing transparency regarding the effect of non-controlling interests on the financial position, financial results and cash flows of the group. None of the companies in the review has disclosed summarized financial information or disclosed the non-controlling interest accumulated at the end of the financial year for each subsidiary with a material non-controlling interest. Only one company provides the information on the result attributable to holders of non-controlling interests for each subsidiary with a material non-controlling interest.

Once these disclosures of non-controlling interests have to be provided, the shareholders in the group can gain a better understanding of the effect of non-controlling interests on the group's financial position, financial results and cash flows, and therefore of the risks faced by the group. The users will thus be better informed regarding the actual value of the assets and liabilities of the non-controlling interests, and also the extent to which the assets and liabilities are attributable to the holders of the non-controlling interests. Furthermore, investors will be better able to distinguish between the company's interests and the interests of third parties. Investors will then be better positioned to form their own opinion regarding the effect of non-controlling interests on the various ratios and items in the financial statements.

The inclusion of these disclosure requirements in IFRS 12 is in the interests of investors. The AFM urges the companies subject to supervision to identify the information that is needed and to provide it prospectively, in order to meet this need for information.

14 (of the 42) companies do not provide a proper description of the composition of the group
A third of the companies do not provide a proper description of the composition of the group. For users of the financial reporting, it is important that they can form an impression of the group's composition so that they can estimate which ownership interests affect - or could affect - the group's financial position, financial results and cash flows.

The AFM has noted that 41 of the 42 companies reviewed are required to include a statement of ownership interests or a reference to the Trade Register in their financial statements. One company is not subject to this requirement, as it is a so-called third-country issuer[1], which has prepared its financial statements on the basis of reporting standards that are considered to be equivalent by the European Commission. Since the requirements of Title 9 Book 2 of the Dutch Civil Code do not apply to third-country issuers, an investor cannot form a true impression of the composition of this company's group.

The AFM moreover notes that 20 companies have included a statement of ownership interests in their financial statements. All companies list the legal entities that are fully consolidated.

16 of the other 21 companies have filed a list of ownership interests with the Trade Register, although only 10 of these 16 companies included a reference to the Trade Register in their financial statements. 8 of these 16 companies do not disclose which legal entities are or are not fully consolidated. In 3 of these 8 cases, the list of ownership interests had not been updated since 2010. Finally, the AFM notes that 5 companies (12%) do not publish a list of ownership interests at all.

Review design
The AFM carried out this thematic review as a baseline measurement, in order to gain an impression to what extent companies already comply with the future requirements and which will help to provide the information needed by investors.
The input for this thematic review was the 2011 financial reporting of 42 companies subject to supervision with the largest non-controlling interests relative to group equity.

[1] *A third-country issuer is a company domiciled outside the EEA with a market listing in the Netherlands.*

2 Key review results

2.1 25% to 50% of the companies have a material (or potentially material) non-controlling interest

In its review, the AFM found that the interests of third parties in one or more group companies (non-controlling interests) form a material part of the total group equity of approximately a quarter of the companies subject to supervision. In addition, the AFM notes that the non-controlling interests measured as part of total group equity are not material for approximately a quarter of the companies reviewed. However, it is possible that these non-material, non-controlling interests could have a material effect on one or more individual items in the financial statements of these companies.

The fact that 25% to 50% of the companies subject to supervision have a material or potentially material non-controlling interest means that transparency regarding the effect of non-controlling interests on the financial position, financial results and cash flows, and thereby the risks of the group, is important to investors.

2.2 Companies are not yet providing transparency regarding the effect of non-controlling interests on the financial position, financial results and cash flows of the group

It is important to investors that companies provide transparency regarding non-controlling interests, because this will give them a better understanding of the effect of the non-controlling interests on the group's financial position, financial results and cash flows, and therefore also the risks faced by the group. Investors will thus be better informed regarding the actual value of the assets and liabilities of the non-controlling interests, and also the extent to which the assets and liabilities are attributable to the holders of the non-controlling interests. Investors will then be better positioned to form their own opinion regarding the effect of non-controlling interests on the various ratios and items in the financial statements. The inclusion of these disclosure requirements in IFRS 12 confirms the fact that this information is relevant for investors.

Currently, companies only need to disclose the totals of the non-controlling interests in the primary statements. This disclosure requirement, however, does not provide any financial information to enable investors to estimate the value of and risks associated with these non-controlling interests. Furthermore, these statements do not provide any information to investors regarding the actual value of the assets and liabilities of the non-controlling interests, and also no information as to the extent to which the assets and liabilities are attributable to the holders of the non-controlling interests. This view is supported by the position paper 'Full consolidation of partly owned subsidiaries requires additional disclosure' by Eumedion that was published in July 2012.

The AFM notes that only one company did not fully comply with these disclosure requirements by incorrectly not stating the proportion of the equity held by the non-controlling interest.

Companies are still not yet required to provide information on each subsidiary with a material non-controlling interest that shows the (potential) effect of these non-controlling interests on the group's financial position, financial results and cash flows.

The expected introduction of IFRS 12, disclosure of non-controlling interests, as of 1 January 2014, will require disclosure of information on the result attributable to the holders of non-controlling interests, the non-controlling interest accumulated at the end of the financial year for each subsidiary with a material non-controlling interest, as well as a summary of financial information for each subsidiary with a material non-controlling interest. The anticipated information required will include cash, other current assets, non-current assets, current liabilities, non-current liabilities, revenue, result, other comprehensive income and total comprehensive income. If companies provide the above information, investors will gain a better understanding of the value of and risks associated with the non-controlling interests.

In its baseline measurement the AFM has noted that none of the companies currently comply with the disclosure requirements of IFRS 12 regarding the (summarized) information on subsidiaries with material non-controlling interests. Moreover, the AFM has noted that none of the companies reviewed have disclosed the accumulated non-controlling interest for each subsidiary at the end of the financial year. Furthermore, only one company has reported the result attributable to the holders of non-controlling interests for each subsidiary with a material non-controlling interest.

The disclosures (which are currently missing in most cases) that provide information on the effect of non-controlling interests on the group's financial position, financial results and cash flows and thereby the risks faced by the group will ensure that users are better informed regarding the actual value of the assets and liabilities of the non-controlling interests. In addition, investors will be able to infer the extent to which these assets and liabilities are not at the company's disposal, since they are ultimately attributable to holders of non-controlling interests. This will make investors able to form an independent opinion regarding the effect of non-controlling interests on the various ratios and items in the statement of financial position. Investors currently do not have a good understanding of the distinction between the company's holdings and the holdings of third parties, while in fact this distinction is very important.

The AFM urges companies subject to supervision to identify the information they will need to provide, and to comply prospectively with the disclosure requirements that will soon apply per subsidiary with a material non-controlling interest.

2.3 14 (of the 42) companies do not provide a proper description of the composition of the group

For users of the financial reporting, it is important that they can form an impression of the group's composition so that they can estimate which ownership interests affect the group's financial position, financial results and cash flows.

Under Dutch law, companies must disclose the legal entities that are fully consolidated. The company may file this listing of the legal entities included in the consolidation separately with the Trade Register. Investors should thus be aware that the financial statements will not (and will not have to) include this information in all cases.

The AFM has noted that 41 of the 42 companies reviewed are required to include a statement of ownership interests or a reference to the Trade Register in their financial statements. One company is not subject to this requirement. This concerns a third-country issuer which prepared its financial statements on the basis of reporting standards that are considered to be equivalent by the European Commission. Since the requirements of Title 9 Book 2 of the Dutch Civil Code do not apply to third-country issuers, an investor cannot form a true impression of the composition of this company's group.

The AFM moreover notes that 20 companies have included a statement of ownership interests in their financial statements. All companies list the legal entities that are fully consolidated.

16 of the other 21 companies have filed a list of ownership interests with the Trade Register, although only 10 of these 16 companies include a reference to the Trade Register in their financial statements. 8 of these 16 companies do not disclose which legal entities are or are not fully consolidated. In 3 of these 8 cases, the list of ownership interests had not been updated since 2010. Finally, the AFM notes that 5 companies (12%) do not publish a list of ownership interests at all.

The AFM urges companies to include an up-to-date list of ownership interests in their financial statements or with the Trade Register, in order to meet the need of investors for the information they require to gain a good understanding of the composition of the group and the (potential) effect on the group's financial position, financial results and cash flows.

3 Rationale, objectives and population

Rationale: new standard on disclosure of non-controlling interests (IFRS 12)

The thematic review is conducted in anticipation of the new standard requiring disclosure of non-controlling interests (IFRS 12) that is expected to apply in the European Union on 1 January 2014. Prospective application of IFRS 12 from 1 January 2013 will probably be permitted.

The relevance of this thematic review is also evidenced by the press release[2] and the position paper[3] published by Eumedion, in which listed companies around the world are urged to provide more extensive disclosures with regard to the item of 'third-party interests'. The disclosures currently required in the primary statements do not provide any information to investors regarding the actual value of the assets and liabilities of the non-controlling interests, and also no information as to the extent to which the assets and liabilities are attributable to the holders of the non-controlling interests.

Objectives

The purpose of the thematic review Disclosure of Non-Controlling Interests is to establish the extent to which companies already comply with the future requirements of IFRS 12.

The key objectives of the review were:

1. How many companies have subsidiaries with material non-controlling interests?
2. To what extent do companies already comply with the future disclosure requirements for non-controlling interests (IFRS 12)?
3. To what extent are the users of the financial reporting in a position to understand the composition of the group, and to what extent are they provided with information regarding ownership interests that influence or could influence the group's financial position, financial results and cash flows?

Population: 42 companies

The thematic review was conducted on the 2011 financial reporting of companies with a listing on a regulated market in the European Union as at 31 December 2011. The 42 companies included in the review are the companies with the largest proportion of non-controlling interests relative to group equity.

[2] *Eumedion press release 5 July 2012 – Companies appear larger than they are to investors – Impenetrable line item in financial statements requires disclosure*
[3] *Eumedion position paper 5 July 2012 - 'Full consolidation of partly owned subsidiaries requires additional disclosure'*

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Amsterdam, October 2012