

S02.02-AS-03-II.7

I - Tangible (and intangible) assets: General principles

6. Elimination of profits in tangible and intangible assets

6.1. General

Profits are included in tangible or intangible assets where **consolidated** Group enterprise A buys tangible or intangible assets for resale to **consolidated** Group enterprise B, at a selling price with a profit margin, thus higher than costs of acquisition or production borne by A.

Such transfers can include:

- Tangible assets constructed by A especially for resale to B (new installations) or used goods, already partially depreciated by A
- Tangible or intangible assets (software, business as a going concern).

Depreciation of the corresponding assets by B done after acquisition will gradually reduce the margin, and it is fully realized only when the asset is entirely depreciated or sold to a third party.

The profits realized during the **internal** transfers of tangible or intangible assets must be neutralized, as well as any later additional depreciation by the acquiring party.

In the case of a loss, test the seller's asset for impairment before the sale.

6.2. Basic principle

Internal sales ★ of tangible and/or intangible assets are based on fair value, i.e. the amount for which an asset could be exchanged between knowledgeable, willing parties in an arm's length transaction.

★ All sales of tangible or intangible assets between divisions within a same legal entity are made at book residual value as this is not really considered as a sale.

The buyer uses this value to record the purchased asset in Group reporting and depreciates it over the life indicated in the material code for this type of asset unless, for technical or economic reasons, that life is expected to be shorter. The asset has then to be depreciated / amortized over that shorter period.

The seller needs to communicate to the buyer the amount of the profit (loss) on the sale.

6.3 Adjustment principles

The profit before tax in tangible or intangible assets will be eliminated in the Group accounts only if the Group share ★ of this profit exceeds 500 kEUR.

★ The values used for adjustments done by Group Accounting and Reporting on sales or purchases of tangible and intangible assets from companies in joint control are adapted to take into account the holding rate by the Group: only the fraction of the profit belonging to the Group is cancelled. For example:

- in the case of a transfer generating a profit of 2.000 by a wholly owned subsidiary (100%) to a jointly controlled company owned at 60%, the profit eliminated by Group Accounting and Reporting is 1.200 (proportional consolidation is applied).
- in the case of a transfer generating a profit of 2.000 by a wholly owned subsidiary (100%) to a 60% owned company over which the Group has full control, 100% of the profit is eliminated centrally (in this case, the full consolidation method is applied instead of the proportional consolidation).

As profits before tax in tangible or intangible assets cannot be eliminated by the legal entity itself, they are eliminated centrally using the following principles:

Step 1 (Centrally)

Profit is eliminated under the heading where the margin was recorded (gain and losses on current or non-recurring sale of fixed assets), and allocated to the selling division.

Offsetting entry: Tangible or intangible assets of the buying division with correlated impact on net results and reserves.

Step 2

By the buyer (adjustment to reporting)

- Elimination from the capitalized amount of the purchase (tangible or intangible assets) of an amount equal to the profit made by the seller with the reserves as offsetting entry.
The transfer headings to the carrying amount of fixed assets and to reserves are used with flow 70.
- The buyer makes the correlative computations of deferred taxes which impact income statement (deferred income taxes related to current year before valuation allowance) and balance sheet (deferred tax assets-gross).

Centrally

In the same period, the postings of the buyer in step 2 are reversed, using the same headings with the opposite sign (transfer to the carrying amount of fixed assets, transfer to reserves, tangible assets, intangible assets, reserves).

Later periods

In later periods, the buyer depreciates/amortizes the purchased item and computes the correlated deferred taxes (deferred income taxes related to current year before valuation allowance, deferred tax assets-gross). The elimination entries are recorded as an adjustment to reporting (see step 2 above).

Example of a transfer of tangible assets between entities

Company A sells to company B tangible assets valued at 10.000 (tangible assets) in A's Books for a price of 11.000. Company A thus realizes a profit of 1.000 on this sale. We assume the seller's profit is taxed at 40% and the buyer's profit at 30%.

The asset life is assumed to be 10 years according to the [material code](#).

Accounting adjustments can be summarized as follows:

Entered by Company code	Selling company A			Buying company B		Buying company B					
	Locally	Centrally	Centrally	Locally	Locally	Locally	Locally				
	that of the company	separate company	separate company	that of the company	that of the company	that of the company	separate company				
	Step 1	Step 1	Step 2	Step 1	Step 2	Step 1	Step 2	Total			
Cash flow statement	Proceeds from the sale of fixed assets	11.000									
				Fixed assets expenditures	-11.000						
Income statement						Cost of goods sold	-1.100	100			
						Normal straight-line depreciation and amortization	-1.100	100			
	Gains and losses on the sale of fixed assets (current or non-recurring)	1.000	-1.000			Current taxes related to current year	330				
	Current taxes related to current year	-400									
				Deferred income taxes related to current year before valuation allowance		300	Deferred income taxes related to current year before valuation allowance		-30		
	Net result	600	-1.000	Net result		300	Net result	-770	70		
Balance sheet	Miscellaneous debtors / Cash & Cash equivalent	11.000									
				Miscellaneous creditors / Cash & Cash equivalent	-11.000						
	Reserves	-600	1.000	-1.000	Reserves		700	Reserves	770	-70	700
	Transfer to reserves			-1.000	Transfer to reserves		1.000	Transfer to reserves			
	Taxes payable	-400									
								Taxes receivable	330		330
					Deferred tax assets-gross		300	Deferred tax assets-gross		-30	-30
	Tangible or intangible assets	-10.000	-1.000	1.000	Tangible or intangible assets	11.000	-1.000	Tangible or intangible assets	-1.100	100	-1000
	Transfer to carrying value of fixed assets			1.000	Transfer to carrying value of fixed assets		-1.000	Transfer to carrying value of fixed assets			