The so-called “External Partners” in the groups of corporations: a model of presentation in the consolidated statements.

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Abstract

This paper studies, on the one hand, theories set out around the consideration of the external partners in the consolidated information and on the other hand, financial models that discuss the convenience of the separation or not of the different elements that form part of the liabilities of the balance sheet of the companies. A Model is proposed, the External Partners Model, which financially argues a certain presentation and processing of such and that, in our opinion, facilitates the analysis of the consolidated financial statements. This model is based on two hypotheses: (1) the economic and financial variables are not independent and (2) the value of the company depends, among other factors, of the type of sources that constitute their capital. These two hypotheses will imply that a separation should be included in the consolidated balance sheet between equity and liabilities as they are different sources of capital and then its separation will give relevant information to its users.

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I. INTRODUCTION

It could be said that Consolidated Financial statements try to reflect with a general perspective, the total amount of resources of a group of companies that are related to each other and put under a common direction. However, the problem that is found, in relation to the concept of Consolidation, is that this one can be understood of different ways according to the approach or interpretation given to consolidated information. Briefly, and even though in later sections these different theories can be subject of a more detailed study, it is possible to say that as for the processing of the consolidated information, there are diverse positions in the doctrine[1] :

a) the one that conceives consolidated financial statements as a prolongation of the parent company's, well-known as Parent Company Theory. This theory is an exposition of a financial character.

b) the one that conceives consolidated financial statements as a reflection of the economic and financial situation of the group, doing without the distinction between dominant and filial or parent or dependent company. Its an exposition of an economic character ant it is known as Entity Theory.

At the moment, accounting theory is divided between these two expositions. Thus, for example, in favour of the first we found:

> "The object of the consolidated statements is to display, basically in benefit of the shareholders and creditors of the parent company, the results of the operations as if the group was a single company with one division or more"[2]

> "The shareholders of the parent company are interested in the consolidated information given by global results of the operations attributables to the investments of the parent company, and in the dividends, funds flows and similar related. For these reasons, it is considered that the Parent Company theory is most appropriate and a useful base of processing."[3]

Corroborating the second exposition we found examples in the European Union:

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[1] The theory considers other positions different from the ones exposed now, which will be taken into consideration in later sections.

[2] American Institute of Certified Public Accountants. *Accounting Research* núm.51 "Consolidated Financial Statements", New York, 1959, paragraph 1.

[3] Accountants International Study Group. "Consolidated Financial Statements", Lebanon. 1972, paragraph. 26. Cited from Cóndor (1988, p.48).

> "…than in the annual accounts of the corporations that form part of a group cannot by themselves gives a faithful image of their situation; therefore, accounts of the group must be settled down to provide a faithful image of the economic unit that is the group…"[4]

The implications derived from the existence of these two doctrinal tendencies are of great importance at the time of reputing the "external partners" as it will be seen in later sections[5].

II. EXTERNAL PARTNERS VERSUS MINORITY INTERESTS

Habitually, in the accounting literature on Consolidation, the participation in the dependent company that does not correspond to the dominant company has received the denomination of minority interests. This is the case of authors like Cea García (1972), Embid Irujo (1987) or Cóndor (1988). There are, nevertheless, some classic authors like Moonitz o Fernández Peña, who talk about the participations that do not belong to the dominant company using the term "minority shareholders" or "external partners", anticipating themselves to the discussion next considered. Thus, for example, Moonitz (1951, p.13) affirms that:

> "In general, presumably, the minority or external stockholders will not receive any information or benefit of the consolidated."

And, on the other hand, Fernández Peña (1961, p.123):

> "To the part of shares that are in third hands can be given diverse denominations of similar significance such as: Minority group participation, Minority group proportion, Interests of the minority stockholders, Minority proportion of wealth, Foreign participation in controlled companies, Proportion of capital and reserves attributables to external shareholders…."

Fernández Peña, in spite of not mentioning the concept of "external partners", does refer to the "proportion of capital and reserves attributables to external shareholders" reason why it can be said that he is considering that there is a series of shareholders who have a part of the capital of the dependent corporations and whose participation does not have to be under 50% for reasons that will be exposed later.

[4] See "Expositions des motives de la Commissión des Communautés Européennes". "Proposition de septieme directive". Journal Officiel des Communautés Européennes. 17th of January, number C,14.

[5] In the introduction (paragraph 2) to the "Normas sobre formación de las cuentas de los grupos de sociedades" (1982), now abolished, the existence of these two doctrinal tendencies is mentioned, evolving in the direction of the first one.

Accounting legislation does not follow any uniform criterion. NIC number 22 (IASC, 1983) refers to the minority interests and defines them as:

> "that part of the results corresponding to the shares in third hands different from the parent company or other subsidiaries in the group".

Nevertheless, the Spanish legislation, and more concretely the "Normas para la formulación de las Cuentas anuales consolidadas" (Standards for the annual formulation of Consolidated Accounts) (article 64) and Law 19/89 of partial reform and adaptation of the mercantile legislation to the directors of the C.E.E. in the matter of corporations (article 45) talk about the external partners.

The denomination of the participation in the dependent corporations that does not belong to the dominant company, as Minority interests does not seem very exact as soon as the adjective "minority" implies that the dominant company owns the major part of the shares whereas the rest of the partners has an inferior participation to the majority. However, and following the rules for the formulation of the consolidated annual accounts, a dominant company is a mercantile company which has most of votes or, has the faculty to name or to dismiss most of the members of the administration advice, reason why effective control could be held with a participation inferior to 50%, that is to say, with a non-majority participation. By all it, and in our opinion in a correct way, the Spanish legislation decided to include the term "external partners", much more agreed with the real situation as long as Spanish legislation identifies itself with the Parent Extension Company (which will be detailed in later sections) by which groups financial statements are considered like a mere prolongation of the financial statements of the dominant company. Nevertheless, it is possible to say that although this denomination of external partners seems to us suitable in the circumstances just described, we would not be in agreement with it in the context of other theories like the Entity Theory (also developed in later sections) in which the denomination of "external" does not correspond with the conception that, under this theory, is held of the diverse elements that compose the liabilities of the consolidated balance sheet.

III. FORMALIZATION OF THE EXTERNAL PARTNERS

For coming to the formalization of the concept of external partners we start from three hypotheses:

a) we only consider the existence of two corporations, a dominant one (D) and a dependent one (d).

b) we consider that between the dominant company (D) and the dependent company (d) a relation of total direct dominion exists.

c) we consider that there are no differences between the value of the investment and the theoretical value of the dependent company, that is to say, we do not consider the existence of “consolidation differences”.

We represent in the first place the patrimonial equation of the dominant company. If we denominate A_D to the dominant company assets, exclusion done of the participation in the dependent company, L_D to its liabilities and E_D to its Equity, we can write:

[1] $$A_D+I_{D/d} = L_D + E_D$$

where $I_{D/d}$ represents the investment of the dominant company in the dependent company.

In the case of the dependent company, and using the same terminology, we will denominate A_d to the assets of the dependent company, L_d to its liabilities and E_d to its Equity, so the patrimonial equation will be represented in the following way:

[2] $$A_d = L_d + E_d$$

In the case that we have proposed, because the dominant company has 100% of the capital of the dependent company, we will be able to affirm that:

[3] $$I_{D/d} = E_d$$

and, therefore, to obtain the consolidated balance we will only have to eliminate both accounts , and the patrimonial equation of the consolidated balance will be the sum of [1] + [2] with the simplification of [3]:

$$A_D + A_d = E_D+ L_D + L_d$$

Instead of considering the hypothesis b), we will now consider the hypotheses d) that may be expressed in the following way:

d) between the dominant company (D) and the dependent company (d) exists a relation of partial direct dominion. If we represent as t the percentage (over 1) of possession of titles of the dependent

company on the part of the dominant company, we can express the patrimonial equation of the dependent company of the following form:

$$A_d = L_d + t^*E_d + (1\text{-}t)^*E_d$$

where $(1\text{-}t)^*E_d$ represents the part of the equity in the dependent company which does not belong to the dominant one, that is, the external partners.

In this case then, the investment of the dominant will no longer be equal to the total equity of the dependent, but to one part and therefore, the items eliminated when consolidating will now be[6]:

$$I_{D/d} = t^*E_d$$

and, therefore, the consolidated patrimonial equation will be:

$$A_D + A_d = L_D + L_d + E_D + (1\text{-}t)^*E_d$$

where $(1\text{-}t)^*E_d$ will reflect, within the liabilities of the consolidated balance, the part corresponding to the external partners. Evidently, this formalization has sense if the consolidation is carried out by the method of global integration, since in the case of the proportional integration the part corresponding to the external partners would no longer appear in the consolidated patrimonial equation (discussion that will be held in later sections). And, as far as the Equity method, there is no integration since it responds to a substitution[7] in monetary terms.

IV. THEORIES RELATIVE TO THE PROCESSING OF THE EXTERNAL PARTNERS.

We may now proceed to the study of the different approaches that, on the matter of the presentation of the external partners have been set out in the accounting doctrine during this last century. To do that, we can first raise a classification of the theories developed until the moment that would be the following one:

- Theories that suggest the participation corresponding to the external partners must appear in the consolidated accounts.

[6] We keep the restrictive hypotheses exposed before stating that the value of the investment is equal to the proportional theoretical value of the dependent company.

[7] "Consolidating is the same as substituting the accounts which represent the investments in a company for the proportional value of this company" (Capella, 1975, p.178).

- Theories that propose the non-appearance in the consolidated balance of the external partners.

With the purpose of showing the existing relation between this classification and the proposed in previous pages when we talked about the different expositions suggested by the doctrine at the time of making the consolidated information, we propose the following scheme:

1. *Entity concept*: inclusion of the external partners. Global integration. This would include the Entity Theory, Parent Company Theory and Parent Company Extension Theory.

2. *Property concept*: non-inclusion of the external partners. Proportional integration or Equity method.

In previous pages, we have talked about both the Entity Theory and the Parent Company Theory when exposing them like two different approaches for the processing and interpretation of consolidated information, in general, no matter the consequences that may have in the external partners. In the present section, we see how these theories of a more general character, are also of application when dealing with a more specific subject like the one studied in the paper

IV.I THEORIES THAT SUGGEST THAT THE PARTICIPATION CORRESPONDING TO THE EXTERNAL PARTNERS MUST APPEAR IN THE CONSOLIDATED ACCOUNTS

They start from the assumption that at the moment of carrying out the consolidation, to the financial statements of the dominant company will be added, not only the part of the dependent corporations that belong to the first but its total wealth. In the Global integration Method, as we have seen before, we find ourselves with a part of the assets and liabilities of the dependent company which do not belong to the dominant company and constitute the external partners. This item will appear, evidently, in the liabilities of the consolidated balance sheet, but the question now is, in which epigraph?. Trying to answer this question implies taking care of the form the consolidated accounts are reputed.

IV.I.I. ENTITY THEORY

This first theory, traditionally denominated Entity theory[8], proposes that the external partners form part of the group equity and therefore must be considered as the rest of the partners ,that is to say, exactly just as the partners of the dominant company. The origin of this theory is due mostly to Paton, (Clark, 1993) who, in 1922 referred to the patrimonial equation in the following terms:

Assets = Liabilities

The main idea of this theory[9], is that the company is an only operative unit, different and independent of its proprietors, who has a set of assets and liabilities. Paton (Clark, 1993) considers that both creditors and shareholders provide the company with capital, reason why in return they receive a compensation. He affirmed that the sources of capital of the company do not affect the operations of the business of the enterprise and that therefore, the differentiation within the balance sheet, between liabilities itself and own funds was not relevant. Authors as Modigliani and Miller (1958) supported this thesis[10], with the Irrelevance Theorem, that gathers the ideas of Paton, giving origin to the Paton/MM model. The main idea of the Paton/MM model is that the structure of the capital is irrelevant. Ant it bases this affirmation on two basic hypotheses:

a) The decisions of financing and investment are independent (the real and financial variables are independent).
b) The value of the company does not depend on the type of capital used in their structure.

Paton argues that the type of capital sources does not affect the performance of the company. If debt is replaced by capital, the cost of the factors of production stays. The operating profit will not be affected by the degree of indebtedness of the company. Therefore, the degree of indebtedness of the company will not affect the decisions of the investors. Already in 1958, Modigliani and Miller proposed that in a world without taxes, the market value of the company is independent of its structure of capital and that, for the investors, is equal to the present value of future cash-flows. This premise is consistent with Paton's theory of organisation. More ahead, Modigliani and Miller (1963) argue, however, that the fiscal deduction of the interests of the debt, increases the value of the company and results in a preference for the debt instead of financing via shareholders' equity.

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[8] Some authors denominate it as Economic Theory.

[9] We are talking about the Entity theory, not referred specifically to the external partners, but included in the Accounting General Theory. What we pretend to do with this paper is connecting Accounting and Finance doctrinal tendencies with the study of the external partners.

[10] Paton (Clark, 1993) described the Entity theory much before de modern development of the capital structure theory which is generally attributed to Modigliani and Miller (1958).

Under the premise of no risk of bankruptcy and whenever it is favourable, a company will always tend to replace actions by debt. This new contribution goes against the theorem of the irrelevance. From the perspective of the investor, if the debt increases until an optimal level, it will be positive for the enterprise. But superior levels of debt could mean future cash problems or even insolvency.

Nevertheless, this new model MM considering the tax effect does not consider the potential impact of asymmetric tax policies. Thus, the benefit waited for by the deduction of interests of the debt can be reduced by personal imposition if the individuals replace personal loans by company loans (Stiglitz, 1969) and, then, the expected benefit of the indebtedness will be the difference between the tax saving by the loans of the company and the saving that will be owed to the individuals if they decide to lend money. In addition, Miller (1977) argued that, independently of the indebtedness level that the company wishes to have, there will always be a natural customer for its shares. Investors with a low level of fiscal retention will buy shares of companies very indebted and the shares of companies with low ratios of debt/equity will be bought by investors with high levels of fiscal retention. Therefore, Miller provides arguments that re-establish the validity of the Modigliani and Miller theorem of irrelevance, consistent with Paton theory.

We can see then that the theories of Paton and MM are consistent. The financial statements will give to all sources of capital of the company a similar processing. The assets of the company belong to this one and not to their partners. The income of the company generated by these assets will not be affected by their later distribution between the capital carriers. The profit and loss account reflects the income of the organisation as a whole and is the later distribution of benefits the one that establishes how it is distributed between the different sources of capital. Because the fundamental distinction between debt and equity does not exist, the balance sheet will only show the relation of balances in favour of the capital suppliers[11].

Evidently, from the moment that it is accepted that when we want to value the company or the investors risk, the type of funds is not a relevant information, then its differentiation is not necessary for the users and the external partners can be considered within equity since simply they will be considered like any other capital source. Authors like Keller (1966, p.263) advocates this processing:

> "In theory the minority interests are clearly part of equity within the balance sheet. The minority interests are not an obligation pending to pay and classify them in the middle of nowhere is simply to avoid the subject"

[11] Paton admits the existence of certain differences between shares and bonds. However he argues that they are alternative financing options.

The consequences of this theory are (Bailly and Lavoyer, 1992): in the first place, that the differences in the acquisition and valuation will be recognised on the basis of the global value of the dependent company, as much in the part corresponding to the dominant company like in which it corresponds to the external partners. Secondly, that the internal results will be eliminated in their totality, by the amount imputed to the dominant company and the external partners based on their respective percentage and, thirdly, the consequence already mentioned, that the external partners will appear like equity capitals.

The patrimonial equation, in the frame of the theory exposed, would be expressed in the following terms:

$$A_D + A_d = L_D + L_d + \underbrace{E_D + (1\text{-}t)^*E_d}_{E_g}$$

where E_g is the group equity.

This way the external partners will be considered as part of the group equity (FP_g)

We would like to emphasise a different alternative that Rosenfield proposes (1986) according to which the external partners are also included in equity but are not detached. This author proposes that the information contained in the equity section is generally classified according to the origin of the fund and therefore we find ourselves with capital on the one hand and with retained benefits or reserves on the other hand. Since the dividends already distributed are discounted of the reserves, the amount of these does not show what the evolution of the company has been, as we could find ourselves with the case of a company with a very favourable results but also with a liberal policy in relation to the distribution of dividends. In this case, the amounts that would appear in the section of equity could be smaller than the one of another company, that with worse results during the last exercises, had decided to carry a more preservative policy retaining the benefits in the company. This demonstrates the amount of equity can often lead to ambiguities when we try to carry out a financial analysis on the basis of the data of the balance sheet. And even if the equity would show the total amount of reserves obtained except the distributed dividends so that in the end we obtained the number of reserves available[12], the amounts shown in the balance sheet would not inform us about the tendency followed by the company in the last exercises.

[12] We avoid here a more detailed analysis of the reserves, and we refer to them as available reserves without distinguishing between the different types of reserves held in the Spanish “Plan General de Contabilidad”.

And that is why it is proposed that equity is shown as a single amount, just like the difference between the total assets and the total liabilities of the company. At the time of processing the consolidated information, the participation in the dependent corporations that does not belong to the dominant one, will appear in the liabilities of the balance sheet within the section of equity like a residual value. The patrimonial equation corresponding to this second alternative would be:

$$A_D + A_d = L_D + L_d + E$$

where E would solely be a residual value that would not provide any information to us.

However this last option would not give users as much information as possible, and that, in our opinion, would be against the true and fair view.

IV.I.II. PARENT COMPANY THEORY

A different alternative is the one proposed by Parent Company Theory or *Teoría de los estados financieros de la sociedad dominante*[13]. The main idea of this theory is that the consolidated financial statements are a mere prolongation of the accounts of the dominant company. The authors who propose this theory could be positioned within the current that considers that the separations between liabilities and equity is relevant and by no means should be avoided in the financial information. An example of that if the model known as Decision-Useful Model (Clark, 1993), which demonstrates that the theorem of irrelevance proposed in the Paton/MM model is not consistent since the indebtedness level and therefore the possible level of leverage does affect the risk and the expected income of the shareholders. They affirm that at a greater level of indebtedness in relation to the level of equity, greater is the risk associated to the possession of shares and therefore greater is the compensation expected by the shareholders. They demonstrate that the proportion debt/equity established by the company can provide investors with signals relative to the expected cash flows and therefore relative to the value the attribute to the company.

Evidently, and as a result of what we have just exposed, they consider that the separations between equity and liabilities is by no means irrelevant and that it must be provided to the users of the financial statements so that they can make rational decisions.

[13] Some authors refer to it as Financial theory.

Once determined that the differentiation between debt and equity must exist, the question will be what elements must be considered either like debt or like equity. Following the present theory, the external partners will appear like any other creditor within the company's liabilities. That is to say, we are considering now that the consolidated balance sheet is made up of series of assets that belong to shareholders of the dominant company and series of obligations (in contrast with the theory of the organisation where the company was an independent being of its shareholders), between whom are the rights that on these assets, have the external partners.

Authors who share this point of view are (1917):

> "The suitable practice is to consider like obligation the shares owned by the minority stockholders"

o Macleod (1981):

> "Any minority interest in the subsidiaries must be shown as the last element within the obligations"

According to this, the consolidated balance sheet patrimonial equation could be written:

$$A_D + A_d = \underbrace{[\, L_D + L_d + (1\text{-}t)^*E_d \,]}_{L_g} + E_D$$

where the external partners are included in the liabilities of the consolidated balance sheet (L_g= group liabilities) as if they were one debt more.

IV.I.III. PARENT COMPANY EXTENSION THEORY

And the third and last possibility considers that the participations of the external partners must appear like a differentiated element that locates itself neither as equity nor like a creditor in the liabilities, but in an intermediate position. This proposal considers, exactly the same as the previous one, that the accounts of the group are a mere prolongation of the accounts of the dominant

company. Therefore, the external partners cannot appear within equity next to the partners of the dominant company. Nevertheless, they also argue they can either be considered like any other creditor and, therefore, they must be treated as "nearly-creditors", appearing in an intermediate section between equity and liabilities. That is to say, considers the external partners as a *sui generis* external financing (Cea García, 1991) for the partners of the dominant company, which is not real external financing as it does not have neither contractual remuneration nor deadline for its reimbursement, but either is own financing. It is a mixed, eclectic position of the two previous ones, given the difficulty to arrive to a consensus as far as the processing of the external partners. Authors who agree with this position are, for example Paton (1941)

> "Minority interests should be shown as a differentiated element between the liabilities and the equity corresponding to the dominant company"

Surprises that Paton, precisely, proposes this processing when he has been one of the precursors of the theory of the organisation according to which external partners presentation is indifferent as they are an origin of resources like any other one. We can see here the little consensus there exists around the external partners processing. The IASC, on the other hand, also advocated this processing in their NIC number 3, now derogated.

On the other hand, and against this third theory, it seems to us interesting to emphasise the contribution of Sapienza (1969, p.505):

> "to locate the minority between creditors and shareholders is similar to send it to the limb"[14] (the translation is ours).

The patrimonial equation corresponding to the consolidated balance sheet would be:

$$A_D + A_d = \underbrace{[\ L_D + L_d\ ]}_{L_g} + \underbrace{[\ (1-t)*E_d\ ]}_{QL_g} + \underbrace{[\ E_D\ ]}_{E_g}$$

where:

L_g: liabilities of the group.

[14] Therefore, the Spanish legislation sends them to the limb.

QL_g: quasi-liabilities of the group.
E_g: equity of the group.

What let's us conclude that, under this theory, the fundamental equation

$$A = P + N$$

must be formalised including in its financial structure a new category (QL) corresponding to the external partners, so:

$$A = L + QL + E$$

We want to make it clear that this split of the liabilities does not arise from a mere qualifying aim, but from an *ex-novo* conceptualisation. This is the presentation required by the model of consolidated balance established by the Spanish norms.

IV.II. THEORIES THAT PROPOSE THE NON-APPEARANCE OF THE EXTERNAL PARTNERS IN THE CONSOLIDATED INFORMATION

We enter here the second group of theories, which considers that the external partners do not have to appear in the consolidated financial statements. This theory has been traditionally known as Theory of the property, and contemplates the company as an assembly of assets and liabilities that belong to the partners. In fact it has in common with the Parent Company Theory and the Parent Company Extension Theory that all of them consider that the organisation is not independent from its shareholders and that consolidated financial statements, the consolidated balance sheet in particular, shows to the property the wealth of the shareholders in a determined moment. The difference between them is that the Theory of the property or Property Concept, considers that at the moment of consolidating, is should only be added to the financial statements of the dominant company, the part that owns of the dependent one and therefore the external partners would not be included in the consolidated balance sheet. And to make that possible, the consolidation takes place according to the method of Proportional Integration[15] .

The authors that advocate this other possibility (Rosenfield, 1986) affirm that:

[15]When Rosenfield (1986) proposes to include the external partners in a "residual" equity where only the difference between total assets and total liabilities would be shown, argues that in this way external partners will not be included in the consolidated balance sheet, but that is not true because, although they are not disclosed, they are included in the total amount, if consolidation has been carried out with the Global integration Method.

> "the consolidated financial statements obtained by means of proportional integration do not display the amount of minority interests and therefore they only inform about the attributes of the dominant company"

V. A PROPOSAL OF A MODEL TO PRESENT AND PROCESS THE EXTERNAL PARTNERS

Next a new model is exposed which will argue financially a certain presentation and processing of these external partners, based in the following hypotheses:

1. Economic and financial variables are dependent: the different financing alternatives affect the operatives costs and therefore the decisions of investment and production depend on the capital structure.

2. If the economic and financial variables are dependent, the ratio debt/equity affects future cash-flows and affects income, and therefore affects the value of the company.

In fact the objective of the present section is to connect the financial models that have been set out in the doctrine in relation to the separation or not of equity and liabilities in the accounting information, and the presentation and processing of the external partners in the consolidated financial statements. The proposed model constitutes a variant of the Decision-Useful Model, and could be denominated as External Partners Model. We frame it within the position (Entity theory) that considers that the consolidated financial statements constitute the representation of the patrimonial and financial situation of an assembly of companies and not only of the dominant company.

On the basis of all the exposed, the main characteristics of the model will be:

a) separation between liabilities and equity. That is, from the moment we affirm that economic and financial variables are dependent and that investment and production decisions depend upon the capital structure, we are ourselves forced without a doubt, to separate, within the balance sheet, between liabilities and equity (both for an individual company or for a group of corporations), since the proportion existing between them provides possible users with relevant information.

b) on the matter of the location of the external partners, we have framed the present model within the positions that considers the company from the point of view of an organisation that, from an assembly of financing sources, has invested in series of assets. According to this position, we

propose to locate externals partners as part of the equity of the group. We think that considering them as long term external financing is not appropriate since there is no contractual remuneration nor deadline for its reimbursement. We do not think either that considering them as short term external financing is appropriate exactly for the same reasons. The intermediate position that proposed that its inclusion as an independent item that was neither equity nor an external financing seems no accurate to us as it can take to confusion to those users little familiarised with the reading and interpretation of financial statements.

c) information in the notes to the annual accounts. Within the note referred to equity, information must be displayed of the part of the equity that belongs to the dominant company and the one that belongs to the external partners. It should be also included the composition of this new item and its meaning.

According to this model, therefore, the consolidated balance sheet structural equation could be represented of the following form:

$$A_D + A_d = L_D + L_d + \underbrace{[\,(E_D + (1\text{-}t)^*E_d\,]}_{E_g}$$

where:

E_g: equity of the group.

We can see then, how this model is registered by a side within the theory of the organisation (Entity theory) and by another like a derivation of Clark's Decision Useful Model, of the theory of financing. We have defined, therefore, a model that financially argues the inclusion of the external partners, within the consolidated information, like part of equity of the group.

Exposed the model, we will next analyse the consequences of each model in relation to the processing and presentation of the external partners. The first model studied has been the Irrelevance Model of Paton/MM, according to which we did not separate the different sources that compose the structure of capital for reasons that were exposed in previous sections. According to this model, the external partners appeared within the liabilities of the consolidated balance but

without distinguishing themselves from external financing. The main consequence that derives from this processing would be that external partners would appear as suppliers of capital without considering the characteristics that distinguish them of other suppliers of financing, as for example, credit institutions. At the time of interpreting consolidated information for the decision making (that we do not have to forget, it constitutes our last and main objective), the user will not have information about the ratio debt/equity and will not be able to know what is the kind of capital structure that the company uses for the financing of its assets and the obtaining of its profit.

The Decision Useful model proposed by Clark considers that the separation between equity and liabilities is relevant from the moment that the ratio debt/equity affects the value of the company and, therefore, the investors decisions. From this hypothesis, the presentation proposed is as an item of external financing, separating them from the rest of providers. The consequences derived from this exposition is that users of the consolidated information will interpret that external partners constitute an obligation for the company, liabilities. This does not seem correct as they do not have contractual remuneration nor deadline for its reimbursement.

And last, we will refer to the External Partners Model. Based on the fundamental hypothesis that the capital structure does affect investment decisions (which totally differs from the Paton/MM model), it proposes the separation of the different sources of capital and the positioning of the external partners like equity, because we consider that the characteristics of the external partners have much more in common with the equity of the dominant company than with any item of the external financing. We also consider that it must be added, within the consolidated accounts, and more in concrete within the consolidated notes to the balance sheet, detail of the equity of the group, informing about its composition. The consequences that are derived from this model are, in our opinion, that users will have available information about the different capital suppliers and also will be able to consider total equity as a whole. In the same way, the information provided in the notes to the balance sheet will allow them to know the part of equity belonging to the dominant company.

VI. CONCLUSIONS

The present work has defined in the first place the concept of consolidated reports, group of corporations and external partners, exposing the conceptual discussion that has been taking place lately about the denomination of the external partners or minority interests. The next step has been the exhibition of the doctrinal theories and financial models provided until today in relation to the separation of the elements in the balance sheet liabilities and which may affect in a direct or indirect way to the presentation and processing of the external partners. This exhibition has been carried out classifying the theories in two groups: those that include the external partners within the consolidated information and those that do not.

From these models and theories, we have proposed an External Partners Model based on the hypotheses that the economic and financial variables are not independent and therefore the investment decisions are related to the financing decisions, and also that the relation between equity and external financing may determine future cash-flows, the company income and the value of the company. From these hypotheses, we considered that liabilities of the consolidated balance sheet must show the opportune separation between equity and external financing and that the external partners should be considered as part of the equity of the group as they have characteristics that make them be as other partners of the company and exclude them from external financing. All it under the optics of considering the group of companies included in the Entity Theory. It is also sets out that in the memory a detail is provided of the separation between equity pertaining to the dominant company and those pertaining to the external partners.

We have used, therefore, a financial argumentation to propose and to justify a certain presentation of the external partners within the consolidated information. From here, we have analyzed the consequences that are derived from the application of each one of the proposed models. The application of the Paton/MM model is based on some hypothesis we do not agree with, since it considers that the perceptions of the investors with respect to the value of the company are not affected by the type of capital sources that this one uses. Decision-Useful Model de Clark proposes the separation within the liabilities of the consolidated balance sheet, of the diverse suppliers of capital, and we agree with it. However this model identifies itself with the Parent Company Theory and then proposes the presentation of the external partners like external partners as if they were any other creditor of the company. We do not agree with this position as the external partners have no assured contractual remuneration or reimbursement date. The External Partners Model, based on the same hypotheses as Clark's Decision-Useful Model, provides users, in our opinion, with a much more accurate information of the real situation of the group of corporations since the consolidated balance sheet will show the separation between equity and external financing and the external partners will be considered as part of the equity of the group. This way, the users of consolidated reports will be able to distinguish between the different sources of capital of the group and that, in our opinion, will make easier their decision making. Therefore, Paton/MM Model and Clark's Decision-Useful Model are rejected. And it will also be put aside the eclectic position of the Parent Company Extension Theory that proposed to consider the external partners like an intermediate issue between equity and external financing. In our opinion, this intermediate position can take to confusion to users little familiarised with the use of accounting information.

There is no doubt that there are many other issues in relation to the external partners which have not been studied in this work, such as the adjustments of the consolidation process as far as the external partners are concerned, the analysis of the consolidated reports or the fiscal effect of the different positions explored in this paper, which we reserve for future investigations open.

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