

Industrial Development Fund, LLC
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IFRS Accounting White Paper v2

October 10th, 2018

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To: Files
From: Industrial Development Fund, LLC
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Subject: Research and Development (R&D) Whitepaper

I. Introduction

In the Industrial sector, new product research and development (“R&D”) programs are time-consuming and costly. As markets have evolved in recent years, profitability of these programs has been constrained as a result of declining rates of return, rising costs, increased difficulty in sourcing innovative solutions, and more stringent government regulations.

Investors are increasingly looking at short-term returns for their investment. Conversely, the underlying programs that are key for the growth of companies in this industry, require significant upfront investment and have no incoming cash flows for several years (typically 2-5 years). Subsequent cash flows are then received in the range of 10-40 years into the future.

Industrial Development Funding, LLC (“IDF”), engages with leading Industrial Companies (“ICs” or “IC” for an individual company) to assist the IC with innovative R&D funding arrangements, which helps reduce the burden of R&D expense for the IC. These arrangements allow an IC to partner with various investors to assist in the funding and to share the financial risks and rewards of the R&D programs.

II. Background

IDF has access to a variety of investors through existing relationships in prior Industrial R&D programs. IDF arranges for ICs to partner with various investors to contribute funding to and share in the financial risks and rewards of the R&D programs. IDF provides effective partnering because it understands the mega-trends creating the need for alternative funding solutions for IC’s and Investors. Industrial trends include public equities managing for short-term gain, banks shunning riskier forms of lending due to regulatory pressure, industrial customers switching spending from CapEx to OpEx, and decaying infrastructure requiring significant investment. Investor trends include infrastructure funds seeing commoditized pricing for traditional asset-backed finance, the search for yield in low interest rate environment, increasing asset correlation in times of financial stress, and capital horizons for PE firms that are insufficient for longer-term infrastructure plays.

In these arrangements, the investor does not actively participate in the operating activities, but provides funding for, and shares in the commercial and technical risks in the R&D, in return for a future revenue interest in the product. The IC is not obligated to reimburse the investor for the funding provided (no downside protection) and any repayment or return to the investor is contingent on achievement of technology specifications, and generation of future revenue from the sale of the products under development (e.g., investor would receive royalty for each product unit sold).

The commercial objective of each arrangement is to receive funding from investors to help reduce the burden of R&D expense while sharing in the risks and rewards of development. This objective may be achieved through a potential funding arrangement that can be brokered by IDF.

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In the proposed funding arrangement, the IC and investor will establish a special-purpose joint venture (“JV”) entity, whereby the investor will contribute funding to the JV. Through the investment in the JV, the investor will be entitled to participate in the future economics of the JV which are contingent on successful R&D. The IC will contribute the R&D services, and/or the Intellectual Property (“IP”) rights to develop new IP or products. The IC may also choose to contribute funding to the JV if agreed upon by the parties.

Benefits of funding arrangements

There are a number of benefits that can be obtained as the result of funding arrangements arising from the aforementioned structures. These benefits are detailed in the below tables.

Why would an IC enter into R&D Funding Arrangements?	
Transfer risk arising from R&D	An IC can transfer of all or part of the uncertainty and commercial risk involved with R&D to others by structuring the funding arrangement in a way that mutually benefits the IC and the investor. The R&D arrangement may be structured in such a way that allows for the following: - Investor’s financial exposure is tied to the development expense (e.g., royalty payment dilution in the event of a cost overrun); - Investor returns tied to commercial success and timing; or - No minimum return is guaranteed for the investor.
Increased investment capacity	An IC can increase available capital which would have been otherwise dedicated to the R&D program for investment purposes, creation or funding of new programs and/or jobs.
Protect debt-to-equity ratio	By securing funding from other investors, rather than issuing debt securities, an IC can avoid debt service expenditures, and the impact on the IC’s debt-to-equity ratio that would result from issuing debt securities.
Less volatile earnings/ratios on the IC level and the program level	An IC’s near-term earnings would be impacted by R&D spend if internally funded. An R&D funding arrangement will help an IC avoid the impact on the entity’s near-term earnings that would result if the IC incurred the related research and development expenses. This will also improve program profitability and program cash flows.
Less volatile earnings per share (“EPS”) ratios	Rather than issuing equity securities, an IC can enter into a R&D funding arrangement to avoid expanding the ownership of the entity and impact on EPS that would result from issuing equity securities.
Increased supplier negotiation leverage	With more capital, an IC may have greater leverage in negotiating with suppliers. Further, if a supplier can use the product being developed to improve their operations, the supplier may provide better terms to the IC as an alternative method of investing in the R&D program.
To retain ownership of IP and control of program	An IC can structure a funding arrangement in such a way that the IC can retain ownership and control of the program, and investors will act in a purely passive capacity, or where the IC retains purchase rights to buy back the IP created by the R&D.

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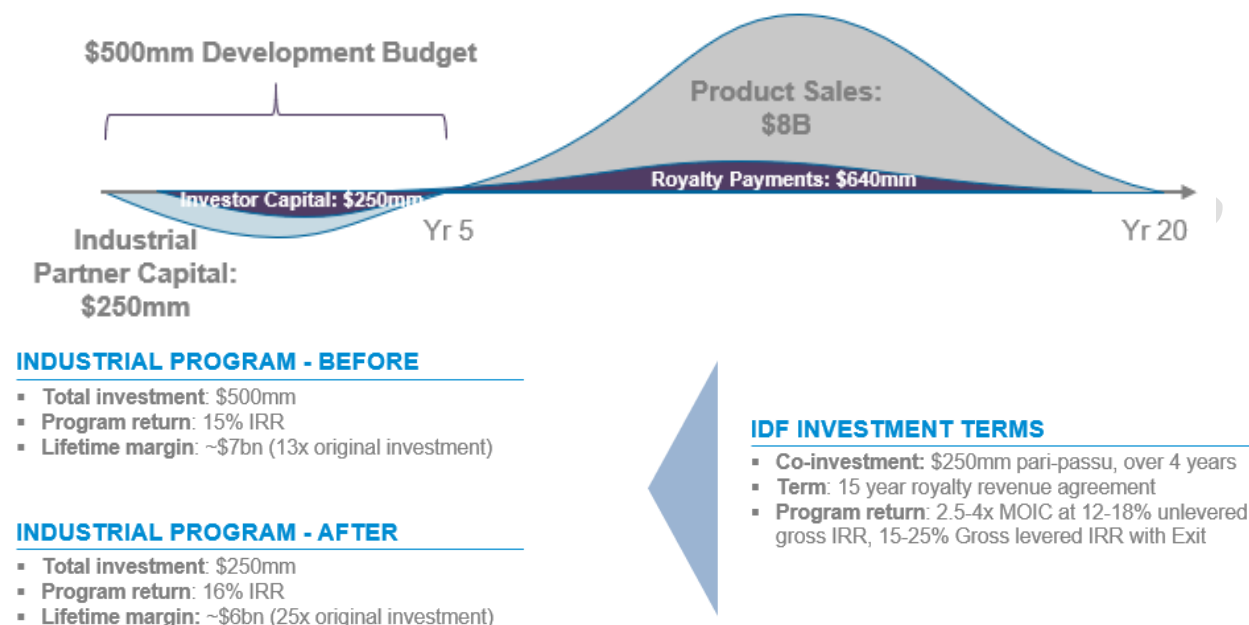
Programmatic and scalable	With an investor funding, the IC is held to a commercially reasonable standard of development, which could be scaled up when the program demands. Additional R&D programs of the IC can be easily added to the structure once the initial R&D program is established.
Why would an investor enter into R&D Funding Arrangements?	
Co-investment in R&D programs with top ICs	Investors have the opportunity to enter into R&D funding arrangement with top ICs that have a reputation or have proven R&D results in the past.
Low correlation to traditional financial markets	Investors may want to diversify their portfolios to include investments in the Industrial sector. This approach takes advantage of the fact that there are very different risk factors affecting Industrial investment returns when compared to the risk exposure in traditional financial markets.
Programmatic and scalable	With an investor funding, the IC is held to a commercially reasonable standard of development, which could be scaled up when the program demands. Additional R&D programs of the IC can be easily added to the structure once the initial R&D program is established.
Tax incentives	Investors may enter into R&D funding arrangements to take advantage of the tax benefits (e.g. tax credits, taxable deductions etc.) that may be offered for the specific R&D services conducted. Tax incentives will be program- and jurisdiction- dependent. Royalty-based nature of structure provides additional tax incentives as royalties carry a 0% tax rate in many of IDF's investor's jurisdictions.

The diagram below displays an illustrative example¹ of the potential economics of the arrangement. This figure shows that the contribution by investors could result in relatively minimal royalty payments compared with the potential for total product sales.

¹ Note, this diagram depicts an illustrative scenario only, however details the simulated economics that could potentially be achieved in a R&D funding arrangement.

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Figure 1: Illustrative economics of an R&D funding arrangement



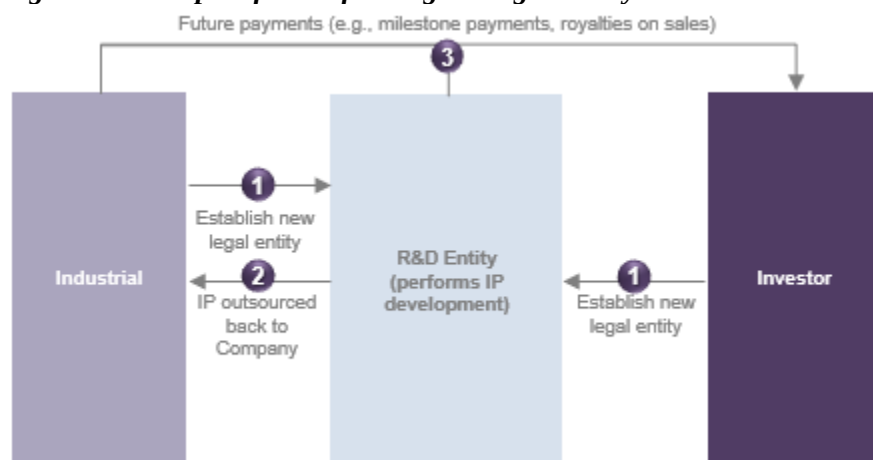
III. Structure

There is a potential transaction structure, with variations therein, that could assist an IC in achieving their commercial objectives. Many recent funding arrangements have included the formation of a new legal entity. Ownership structure of this new entity can vary, depending on the arrangement, and the desired accounting outcome (refer to Section IV. Accounting Considerations for further detail). Under this type of arrangement, the IC, the investor, or both parties establish a new legal entity (“R&D Entity”) which is created with the explicit purpose of performing the R&D activities.

The IC may contribute funding, IP for R&D purposes, and any other necessary resources to the R&D Entity, whereas the investor will contribute funding and may assume a passive role in the operations of the R&D Entity. The IC may retain the IP used in the R&D Entity’s R&D activities, and can also potentially retain the IP resulting from the R&D Entity through provisions established upon the creation of the R&D Entity, or through a purchase option over the IP resulting from the R&D activities. The R&D Entity may also engage the IC for the execution of the IP R&D services to be performed in connection with the R&D program. Returns for investors are contingent on the successful completion of the IP development.

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Figure 2: Example of R&D funding arrangement by JV



Considerations for transfer of risk

To achieve desired commercial results and accounting treatments, careful consideration is required to determine whether an IC has truly transferred financial risk involved with the R&D program to an investor. If financial risk has not been transferred and is not substantive and genuine, it is presumed that an IC has the obligation to repay the funds provided by the investor regardless of the outcome of the R&D. In such cases, the funds received by the investor constitute a liability of the IC and thus cannot be recognized in the Income Statement (i.e. recognized on the Balance Sheet as a financial liability).

While technical risks are the most relevant to the analysis of risk transferred for R&D arrangements, operational and commercial risks will need to be evaluated as to whether these risks are assumed by the investor. These risks are considered in each unique R&D funding arrangement, and no one risk factor is determinative; individual facts and circumstances of each R&D funding arrangement should be considered. This may include (though is not limited to) analysis of the following factors:

- Whether development spending for the program has a clear start and end point, tied to market based clear technical requirements;
- Whether risk associated with achieving technical requirements is medium to high (*refer to Figure 3*);
- Whether there is a risk that the R&D product does not meet specifications;
- Whether there is salvage value to the IP in the event of failure;
- Whether there is a possibility the product could fail before clearing required approvals (regulatory or otherwise);
- Whether the R&D spend would be complete prior to the first unit sales; and
- Whether a clearly defined revenue stream exists that can be tied directly to sales of the IP product.

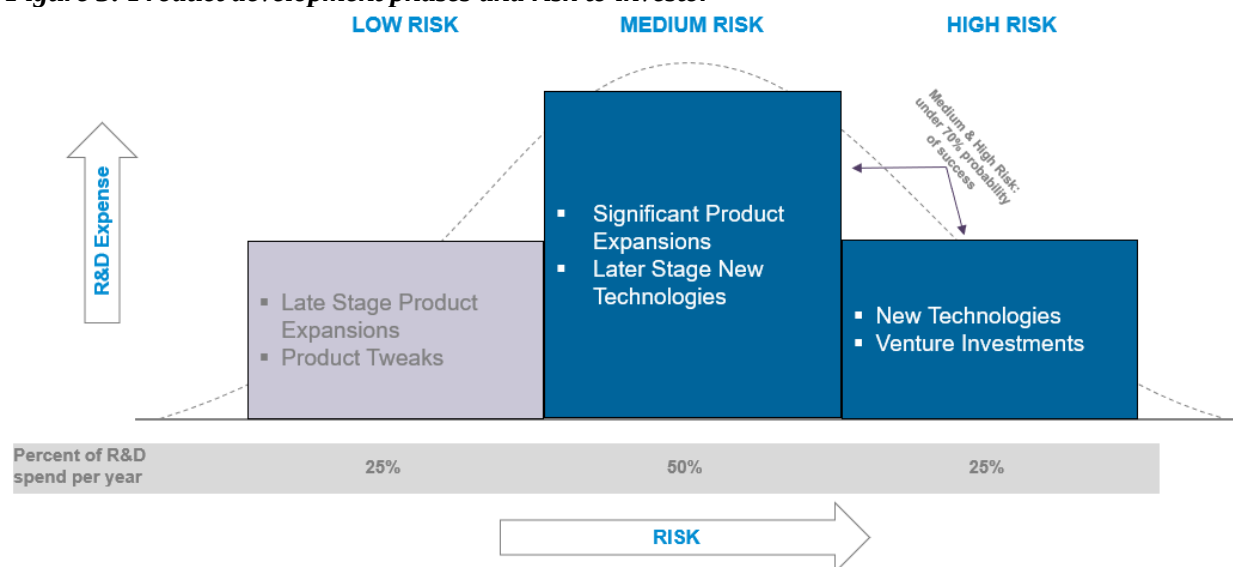
The stage of completion of the R&D program may also be indicative as to whether the R&D will produce IP where realization of future economic benefits is probable. Typically, the later the R&D program phase, the less risky the R&D program, as the IP is typically more developed and tested in later program phases. Further, there are different risks associated with the type of product being developed. For instance, if an R&D program is based primarily on the technology of existing products (“derivative program investment”), this is likely to create a lower risk profile than R&D programs which are attempting to create new products/IP that are not currently in existence. Phases in an R&D program life are detailed below and in Figure 3.

- Low Risk: Tail-end of derivative program investment

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- Medium Risk: Inception of derivative program investment
- High Risk: New program investment

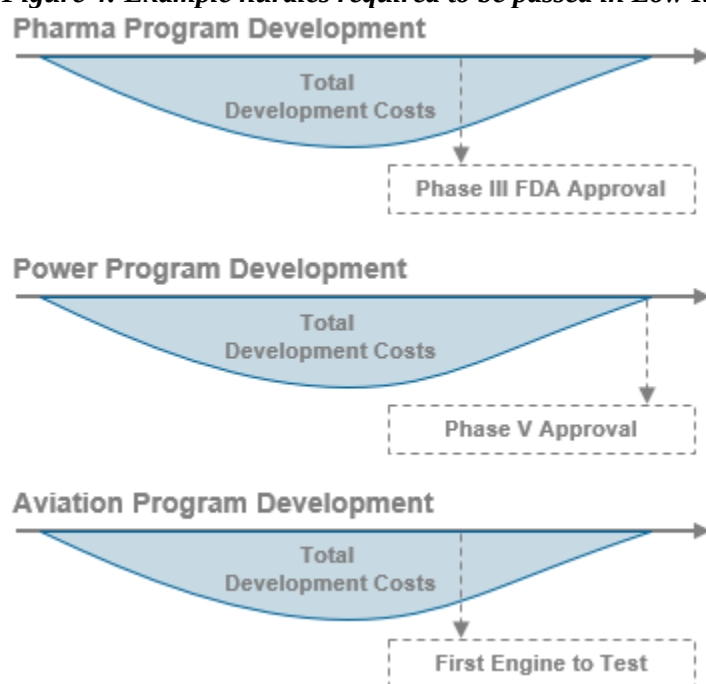
Figure 3: Product development phases and risk to investor



Investment should be made before technological success is guaranteed to transfer substantive and genuine R&D risk to the investor. While investment in medium- to high-risk R&D programs may indicate that an investor is assuming risk without a high probability of successful completion of the R&D into IP, there are situations where an investor enters into a R&D funding arrangement in the Low Risk R&D program phase, where they are able to demonstrate that transfer of financial risk is substantive and genuine. For example, there may be a ‘hurdle’ requirement that the IC or R&D Entity needs to pass before being able to realize the economic benefits of the IP (i.e., there is a chance the IP product will not pass the hurdle requirement and therefore economic benefits may not be able to be realized). Thus in such a situation, risk transferred to investors funding the R&D program prior to the hurdle requirement being satisfied could demonstrate a substantive and genuine transfer of risk to the investor.

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Figure 4: Example hurdles required to be passed in Low Risk R&D program phases



IV. Accounting Considerations

While the benefits of an R&D funding arrangement have been outlined in Section II, an IC should also consider the related accounting impacts of the arrangement as the funding received could have various accounting recognition outcomes: liability, non-controlling interest, income, etc. An IC should understand the risks associated with the R&D program being funded, as well as the obligations of the IC to the investor. These factors may inform the IC's decision about which accounting literature is applicable to the R&D funding arrangement and ultimately the accounting and financial reporting treatment.

The following outlines the accounting considerations for these arrangements in accordance with International Financial Reporting Standards ("IFRS") or International Accounting Standards ("IAS") as detailed below.

Specific facts and circumstances for each R&D program will need to be considered to determine the actual accounting and financial reporting for R&D funding arrangements.

Accounting Guidance

- IFRS 10 *Consolidated Financial Statements*
- IFRS 12 *Disclosures of Interest in Other Entities*
- IAS 32 *Financial Instruments: Presentation*

Accounting Questions

1. How should the R&D Entity account for a funding received from the investor?
2. Does the IC consolidate the R&D Entity?
3. How should the IC account for the consolidation of the R&D Entity, if required?

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Accounting Question 1: How should the R&D Entity account for a funding received from the investor?

The funding received by the R&D Entity from the investor will likely be in exchange for an ownership interest in the R&D Entity. The following analysis provides an overview of the accounting considerations relating to the issuance of an equity instrument by the R&D Entity in exchange for cash funding from the investor.

An instrument is classified as financial liability or an equity instrument in accordance with the substance of the contractual arrangement and the definition of a financial liability and an equity investment. An instrument is classified as a financial liability if it contains a contractual obligation to transfer cash or another financial asset to another entity. While an obligation to transfer cash may arise from a requirement to repay principal and interest, other instruments (e.g., puttable shares or instruments that obligate the entity to deliver a pro rata share of net assets upon liquidation) require careful analysis.

In general, an equity instrument is any contract that evidences a residual interest in the assets of an entity after deducting all of its liabilities and there is no contractual obligation to deliver cash or other financial asset to the investor. However, an exception to the general principles, puttable instruments or instruments that obligate the entity to deliver a pro rata share of net assets only upon liquidation are classified as equity instruments only if certain conditions are met.

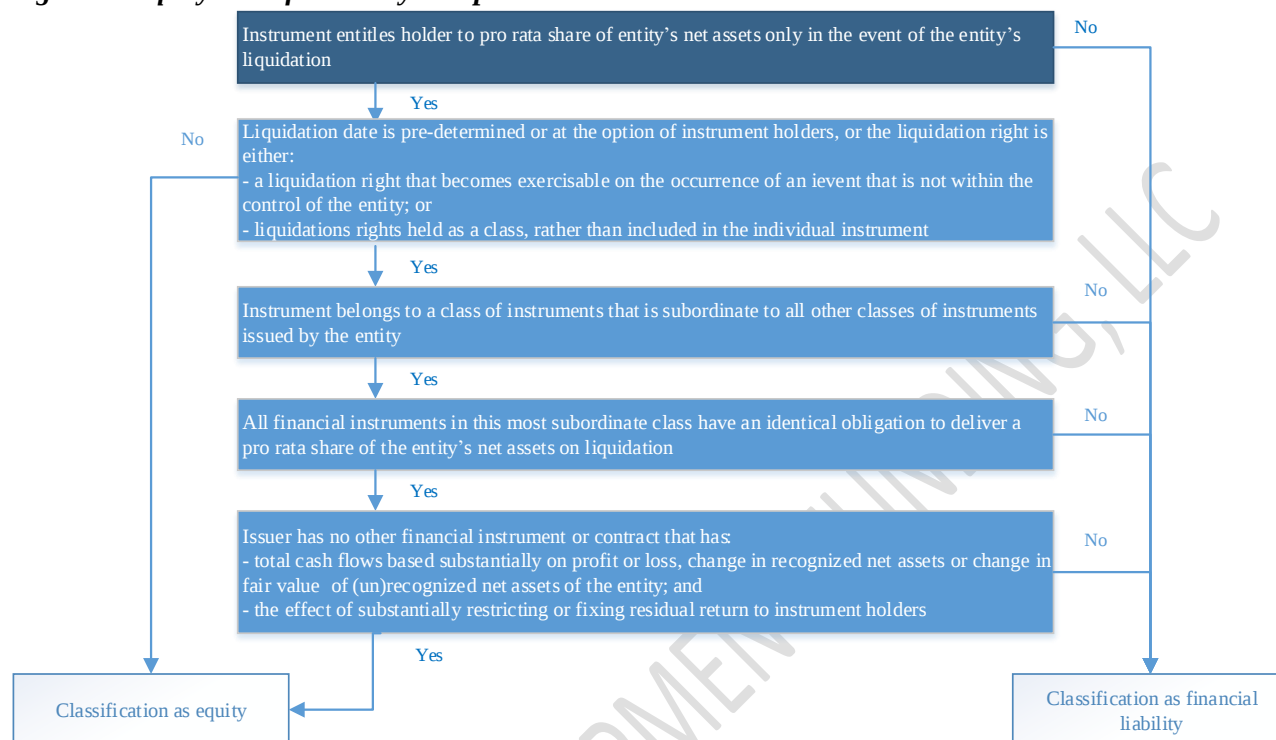
As the equity interest issued to the investor is not intended to be puttable further evaluation of such criteria has not been included. However, the investor, as the holder of the equity interest, may be entitled to its pro rata share of the R&D Entity's net assets upon liquidation. If the obligation to distribute the R&D Entity's net assets arises only on liquidation that is either:

- certain to occur and is outside the control of the entity (e.g., a limited-life entity); or
- uncertain to occur but is at the option of the instrument holder (e.g., some partnership interests);

then the analysis depicted in Figure 6 would be required.

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Figure 6: Equity classification by exception decision tree



If the R&D Entity is a limited-life entity (i.e., liquidation date is pre-determined), or the decision to liquidate the R&D Entity is unilaterally held by one party (i.e., is at the option of any single instrument holder), the financial instrument may meet the exception criteria to be classified as equity.

It is IDF's intention to structure the arrangement in such a way that achieves equity classification.

Additionally, in order to support the conclusion that a financial liability does not exist, there must be no substantive or genuine contractual obligation to settle or repay the investor funds. In circumstances where R&D Entity has committed to repay any of the funds provided by the investor regardless of the outcome of the R&D, the funding received would be recorded by the R&D Entity as a liability, even if the legal form of the instrument is an equity interest. For example, if payment is required upon the occurrence or non-occurrence of uncertain future events that are beyond the control of both the R&D Entity and the investor, the instrument would likely be classified as a financial liability.

Where the instrument contains such contingent settlement provisions, the R&D Entity does not have the unconditional right to avoid making payments. However, if the R&D Entity has control over the contingency that would result in the ability to prevent repayment, there may be a justification that the R&D Entity does not have a contractual obligation to deliver cash or another financial asset to another entity. Said another way, if the R&D entity has the power to avoid repayment, the investor contribution may not be considered a financial liability.

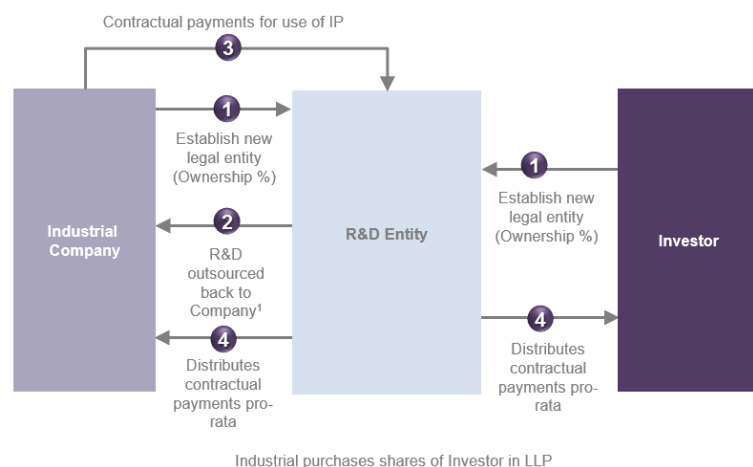
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With regards to the transactions summarized herein, it is intended that the transactions will not have any of the above noted characteristics, thereby further supporting that the funding be equity classified by the R&D Entity.

Accounting Question 2: Does the IC consolidate the R&D Entity?

When an R&D funding arrangement involves the formation of a legal entity, consideration must be given to the consolidation guidance in IFRS 10 to determine whether the IC is required to consolidate the legal entity. A detailed evaluation of the specific facts and circumstances in each R&D program will need to be considered to determine the consolidation conclusion. The following depicts an illustrative example of a JV transaction.

Figure 5: Example of R&D funding arrangement



Note: (1) Other potential prior IP licensing may be required from IC to R&D Entity

The above diagram assumes the following for purposes of presenting an illustrative example:

- The R&D Entity is owned by the IC and by the investor;
- The IC provides R&D services to the R&D Entity at market rates;
- Neither party has any call or put options on the others equity interest in the JV;
- The IC does not have a call option on the R&D if developed;
- If the R&D program is successful, the R&D Entity will own the IP and the IC will license the IP from the R&D Entity in exchange for royalty payments;
- The IC and the investor are not related parties; and
- Accounting is performed in accordance with IFRS at both the IC and the R&D Entity.

IFRS 10 states that an investor should determine whether it is a parent, through an assessment of whether it controls the investee, in this case the R&D Entity. Therefore, the IC will be required to evaluate the provisions of IFRS 10 to determine if it is required to consolidate the R&D Entity.

An IC would be deemed to control an R&D Entity if it has all the following:

a) Power over the investee

The first requirement for control relates to power. An IC will have power over the R&D Entity when it has existing rights that give it the current ability to direct the relevant activities. This requires the careful

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consideration of the relevant activities and the existing rights. Analysis of this criterion would also consider whether R&D Entity is established as a structured entity², where control over the R&D Entity may be evidenced through rights other than equity voting rights.

Structured entities may have some or all of the following features:

- Restricted activities;
- A narrow and well-defined objective such as:
 - Carrying out research and development activities;
 - Funding an entity;
 - Providing investment opportunities for investors by passing on risks and rewards associated with assets to investors;
- Insufficient equity to finance its activities without subordinated financial support; or
- Financing in the form of multiple contractually-linked instruments to investors that create concentrations of credit or other risks (tranches).

Given the purpose and design of the R&D Entity, it is likely that the JV established will be a structured entity. Therefore, when considering whether the IC has power, careful consideration must be given to all arrangement with the entity and not simply the voting rights held via equity interests.

b) Exposure, or rights, to variable returns from its involvement with the investee

The second criterion is to determine whether the IC has exposure (or rights) to variable returns from its involvement with the R&D Entity. The IC is exposed to variable returns from its involvement with the R&D Entity when its returns have the potential to vary based on the R&D Entity's performance, which may be positive, negative, or both.

Examples of exposures to variable returns include:

- Returns from potential commercialization of a product;
- Returns from the development and sale of an asset;
- Fees and exposure to loss from providing credit or liquidity support;
- Residual interests in the investee's assets and liabilities upon liquidation;
- Tax benefits and access to liquidity that an investor has from its involvement with the investee; or
- Economies of scale, cost savings, scarce products, proprietary knowledge, synergies, or other exposures to variable returns that are not available to others.

Depending on the purpose and design of the JV arrangement, when the IC receives returns that are not generated by the R&D Entity, but which stem from involvement with the JV arrangement, these returns are also considered.

c) The ability to use its power over the investee to affect the amount of the investor's returns

The third criterion requires that the IC also have the ability to use its power over the R&D Entity to affect the amount of the returns. This linkage is essential for the IC to be deemed to have control over the R&D Entity and be required to consolidate.

² Per IFRS 12, a structured entity is an entity that has been designed so that voting or similar rights are not the dominant factor in deciding who controls the entity, such as when voting rights relate to administrative tasks only and the relevant activities are directed by means of contractual arrangements.

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If the IC should determine that decision-making rights over the relevant activities of the R&D Entity have been delegated to the IC, it should be assessed whether the decision making rights are being held for the benefit of the IC (i.e. decision-making rights are held in a principal capacity) or the investor (i.e. decision-making rights are held in an agent capacity). The evaluation of the decision-making capacity will determine whether the decision-maker has control that can be used to generate returns for itself and therefore, whether this criterion is met.

If the IC is acting as agent, it cannot have control over the R&D Entity, as there is no linkage between the power and ability to generate returns, therefore it does not consolidate the R&D Entity. However, if the IC is a principal, the IC has the power to direct the relevant activities of the R&D Entity to generate returns for itself, and therefore may have control over and be required to consolidate the R&D Entity.

This is especially relevant when the R&D Entity is set up and the IC is delegated powers by the other investors to direct the activities of the investee on behalf of all investors. Assessing whether the IC is making decisions as a principal, or simply carrying out the decisions made by all the investors (i.e., acting as an agent) will be critical to assessing control.

The following table provides some factors to consider when evaluating whether the IC is required to consolidate the R&D Entity under the provisions of IFRS 10 summarized above.

Control criteria	Applicability to IC
a) Power over the R&D Entity	Power must be demonstrated through the IC's ability to direct the R&D Entity's <i>relevant activities</i> (i.e., those activities that most significantly affect the R&D Entity's <u>returns</u>). Specifically for the R&D Entity, and assuming no IP has been successfully developed (i.e., IP pre-commercialization stage), these activities may include, but are not limited to, the following: - management of research and development activities; - acquisitions and disposals of operating assets; - determination of the funding structure; or - establishing operating and capital decisions (e.g., budgets) and appointing, remunerating, and terminating key management personnel or other service providers. This analysis would also consider whether decisions over relevant activities are made through voting rights, or non-voting rights. Typically, if the party with majority voting rights can exercise these rights over the relevant activities of the R&D entity, this would demonstrate that power is conveyed through voting rights. However, if decisions are made through voting rights, other voting contractual arrangements should also be considered. For example: - if the investor had majority voting rights, however deferred to the wishes of the IC with respect to voting, the IC may be considered to have power; - if the R&D service arrangement between the IC and the R&D Entity covered all the relevant activities, the IC may be considered to have power. If voting rights are not relevant to the determination of power (i.e., not substantive voting rights), the IC may have power over the R&D Entity conveyed through:

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	- evidence of the IC's practical ability to direct the relevant activities of the R&D Entity (e.g., appointment and approval of the R&D Entity's key management personnel); or - special relationships (e.g., if the R&D entity operations are dependent on critical technology or existing IP owned by the IC, or a significant portion of the R&D Entity's activities are conducted on behalf of the IC).						
b) Exposure, or rights, to variable returns from its involvement in the R&D Entity	When the IC's interest in the R&D Entity is via debt or equity instruments, the IC is presumed to be exposed to variability of returns from its involvement with the R&D Entity. Below are some additional examples of exposure to variability that may be relevant: <table border="1"> <thead> <tr> <th>Situation</th><th>Example of IC exposure to variable returns from the R&D Entity</th></tr> </thead> <tbody> <tr> <td>R&D Entity has an IP license over IP owned by IC</td><td> - Revenue earned from the use of license by granting the license - IC access to proprietary knowledge or synergies gained from further development by the R&D Entity </td></tr> <tr> <td>IC provides R&D or management services to R&D Entity</td><td> - Compensation for services rendered by IC (e.g., milestone payments contingent on achievement on specified targets) </td></tr> </tbody> </table> It is presumed that the IC will have met at least one of the situations above, and thus this criterion is likely to be met.	Situation	Example of IC exposure to variable returns from the R&D Entity	R&D Entity has an IP license over IP owned by IC	- Revenue earned from the use of license by granting the license - IC access to proprietary knowledge or synergies gained from further development by the R&D Entity	IC provides R&D or management services to R&D Entity	- Compensation for services rendered by IC (e.g., milestone payments contingent on achievement on specified targets)
Situation	Example of IC exposure to variable returns from the R&D Entity						
R&D Entity has an IP license over IP owned by IC	- Revenue earned from the use of license by granting the license - IC access to proprietary knowledge or synergies gained from further development by the R&D Entity						
IC provides R&D or management services to R&D Entity	- Compensation for services rendered by IC (e.g., milestone payments contingent on achievement on specified targets)						
c) The ability to use its power over the R&D Entity to affect the amount of the IC's returns	If the IC has the power to direct the activities of the R&D Entity in a manner that it can generate returns for itself, then it is a principal and therefore would consolidate the R&D Entity. The analysis of this criterion considers factors such as: - The scope of the decision-making authority of the IC; - Strength of kick-out rights (if any) - The IC's aggregate economic interest in the R&D entity, including any remuneration for services rendered, plus any exposure to variability through other interests (e.g., debt or equity instruments in the R&D Entity). - Remuneration for IC services provided to the R&D Entity and whether these are at market. The linkage analysis is always relevant when applying the control model, but similar to the variability test in criterion b. Only in certain scenarios (e.g., whether a fund manager has control, or if there is otherwise explicit delegation of power), would more detailed analysis of this criterion be required. Outside of the certain scenarios, the default presumption is that the linkage test is met.						

In light of the above, it is likely that the IC controls the R&D Entity, and thus would be required to consolidate the R&D Entity.

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Accounting Question 3: How should the IC account for the consolidation of the R&D Entity, if required?

When the R&D Entity is required to be consolidated by the IC, all intercompany transactions (e.g., R&D service arrangements) should be eliminated in the consolidated financial statements.

If the investor funding is considered equity by the R&D Entity (*see Accounting Question 1 for liability/equity analysis*), the IC would record a non-controlling interest (“NCI”), which would represent the equity in the R&D Entity that is not attributable to the IC. Upon the initial recognition of NCI, the IC should record the amount of NCI for the value of the funding provided by the investor.

The IC would present NCI within equity, separately from the equity of the owners of the IC. Income, expenses, assets and liabilities will be reported in the IC's consolidated financial statements at the consolidated amounts, which will include the amounts attributable to the owners of the IC and NCI. In the IC's consolidated statement of profit or loss and Other Comprehensive Income, the amount of profit or loss and total comprehensive income attributable to owners of the IC and NCI are shown separately; they will not be presented as an item of income or expense.

If the investor funding is considered a financial liability, the cash received is recorded as a liability by the IC and initially measured at fair value (typically the transaction price) and is subsequently re-measured at amortized cost. Interest expense will also be required to be recognized for financing costs using the effective interest rate method.

V. Example Programs

IDF is of the belief that examples 1 & 2 would achieve P&L offset with accounting below and example 3 would not achieve P&L offset:

	1. Next Gen Aircraft Engine	2. Next Gen Turbine	3. Minor Upgrade Package for Turbine
Description	- Development of large commercial aircraft engine with new units sales targeted of +1,500 globally - Will result in most fuel-efficient engine on a per-pounds-of-thrust basis - Designed to achieve significant fuel burn savings over its predecessor - Significant improvements to hot section and inclusion of ceramics parts for first time	- Repowering opportunity to develop the next generation turbine for a large existing Industrial fleet base of 1,200+ units globally - High efficiency, low cost turbines heavily desired for distributed power generation (supporting growth in renewables and smart micro grids) and LNG applications - Significant improvements to hot gas path and compressor	Minor upgrade to existing Industrial turbine with little technological risk
Geography	Global	Global	Global
Program Development Budget	\$5bn	\$240mm	\$20mm
Program Development Period	10 years	6 years	2 years

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Commercial Period	20 year unit sales period (1,500 units, 0% Margin) 50 year service and spare part sales period (20% Margin)	20 year unit sales period (~360 units, 20% Margin) 50 year service and spare part sales period (50% Margin)	20 year service and spare part sales period
Technical Risk	Medium / High	Medium / High	Low
Commercial Risk	High	High	Low
Structure	- JV method - Full risk share - No downside protection (possibility of full principal loss) - No put/call option	- JV method - Full risk share - No downside protection (possibility of full principal loss) - No put/call option	- Debt method - Full risk share - Partial risk share-minimum return downside protection - Put option
Investors	- Financial investors with no strategic links to manufacturer - Royalty based (paid based on units sold, no share of service revenues)	- Financial investors with no strategic links to manufacturer - Royalty based (paid based on units sold, no share of service revenues)	- Financial investors with no strategic links to manufacturer - Royalty based (paid based on units sold, no share of service revenues)
Desired outcome	NCI improvement (JV method)	NCI improvement (JV method)	Amortization of debt

VI. Example T-Accounts

JV Method*

SETUP STRUCTURE

- Record cash received from LLP for future R&D spending

<i>Balance Sheet</i>	
Cash	
① \$250	
Equity – NCI	
	\$250 ①

Net Income/(loss): \$0

R&D EXPENSE

- Industrial incurs R&D expense
- Allocate R&D expense to NCI

<i>Balance Sheet</i>	
Cash	
	\$500 ②
Equity – NCI	
③ \$250	
<i>Income Statement</i>	
R&D expense	
② \$500	
NCI Share of Income	
	\$250 ③

Net Income/(loss): (\$500)
Amount attributable to NCI: (\$250)

SELL PRODUCT & PAY ROYALTIES

- Record revenues from sales over life of Project
- Pay royalty to LLP and distribute to Investor over life of Project

<i>Balance Sheet</i>	
Cash	
④ \$8,000	\$640 ⑤
Equity – NCI	
⑤ \$640	\$640 ⑤
<i>Income Statement</i>	
Revenue	
	\$8,000 ④
NCI Share of Income	
⑤ \$640	

Net Income/(loss): \$8,000
Amount attributable to NCI: \$640

*subject to specific facts and circumstances of JV scenario

Industrial Development Fund, LLC
Research & Development

Debt Method

SETUP STRUCTURE

- ① Record cash received from investor for future R&D spending as debt

<i>Balance Sheet</i>	
Cash	
① \$250	
Debt	
	\$250 ①

Net Income/(loss): \$0

R&D EXPENSE

- ② Industrial incurs R&D expense

<i>Balance Sheet</i>	
Cash	
	\$500 ②
<i>Income Statement</i>	
R&D expense	
② \$500	

Net Income/(loss): (\$500)

SELL PRODUCT & PAY ROYAL TIES

- ④ Record revenues from sales over life of Project
⑤ Pay amortize debt as it is repaid through unit sales of program

<i>Balance Sheet</i>	
Cash	
④ \$8,000	\$640 ⑤
<i>Income Statement</i>	
Revenue	
	\$8,000 ④
Interest Expense	
⑤ \$640	

Net Income/(loss): \$7,360