

## Board Meeting Agenda

Wednesday 13 September 2017

World Champions Team Room, Heritage Hotel, 35 Hobson Street, Auckland

Est Time	Item	Topic	Objective		Page
<b>A: NON-PUBLIC SESSION</b>					
<b>Preliminary</b>					
9.30 am	1	<b>Welcome and Introduction</b> Apologies New member introduction			
9.40 am	2	<b>Board Management</b>			
<b>B: PUBLIC SESSION</b>					
<b>Financial Reporting Framework</b>					
10.20 am	3	<b>Amendments to XRB A1 (Tier 4)</b>	(LWN/VSF)		
	3.1	Cover Memo	Consider	Paper	
	3.2	Draft 2017 Amendments to XRB A1	Approve	Paper	
	3.3	Memo – Proposed Amendments to Tier 4 PBE Accounting Requirements	Consider	Paper	
10.30 am		Morning tea			
<b>For-profit Items for Consideration</b>					
10.45 am	4	<b>Principles of Disclosure</b>	(DB/LK)		
	4.1	Cover Memo	Consider	Paper	
	4.2	Draft Comment Letter	Approve	Paper	
	4.3	Submission Received – Bill Jamieson	Note	Supp paper	
<b>C: NON-PUBLIC SESSION</b>					
11.25 am	5	<b>The Future of Financial Reporting</b>			
12.30 pm		Lunch			
<b>D: PUBLIC SESSION</b>					
<b>PBE Items for Consideration</b>					
1.20 pm	6	<b>Service Performance Reporting</b>	(LK/JS)		
	6.2	Cover Memo	Consider	Paper	
	6.3	Analysis of submissions received	Consider	Paper	

Est Time	Item	Topic	Objective		Page
	6.4	Submissions received			
	6.4.1	R1 Trade Aid Importers Ltd	Note	Supp paper	
	6.4.2	R2 Carolyn Cordery	Note	Supp paper	
	6.4.3	R3 RSM	Note	Supp paper	
	6.4.4	R4 The Treasury	Note	Supp paper	
	6.4.5	R5 CA ANZ	Note	Supp paper	
	6.4.6	R6 OAG and Audit NZ	Note	Supp paper	
	6.4.7	R7 Cherrie Yang	Note	Supp paper	
	6.4.8	R8 Commerce Commission and the Electricity Authority	Note	Supp paper	
	6.4.9	R9 IOD	Note	Supp paper	
	6.4.10	R10 EY	Note	Supp paper	
	6.4.11	R11 Auckland Council	Note	Supp paper	
	6.5	Draft PBE FRS XX Service Performance Reporting	Consider	Paper	
	6.6	Letter to constituents: May 2017	Note	Supp paper	
	6.7	Feedback Statement on 2016 ED	Note	Supp paper	
	6.8	The accountability information needs of key charity funders	Note	Supp paper	
2.00 pm	<b>7</b>	<b><u>PBE IPSAS 40 PBE Combinations</u></b>	(ALH/JS)		
	7.1	Cover Memo – Issues	Consider	Paper	
	7.2	Draft ED PBE IPSAS 40 – marked-up	Consider	Paper	
3.00 pm	<i>Afternoon tea</i>				
3.15 pm	<b>8</b>	<b><u>IPSASB CP Financial Reporting for Heritage in the Public Sector</u></b>	(JP/AH)		
	8.1	Cover Memo	Consider	Paper	
	8.2	Draft Comment Letter	Approve	Paper	
		Submissions received			
	8.3	NZ Police Museum	Note	Supp paper	
	8.3.1	Respondent 1	Note	Paper	
	8.3.2	Respondent 2	Note	Paper	
	8.4	IPSASB CP Financial Reporting for Heritage in the Public Sector – At a Glance	Note	Supp paper	
	8.5	IPSASB CP Financial Reporting for Heritage in the Public Sector	Note	Supp paper	

Est Time	Item	Topic	Objective		Page
3.45 pm	<b>9</b>	<b><u>IPSASB CP Revenue and Non-Exchange Expenses – Project and Outreach Plan</u></b>	(ALH/AH)		
	9.1	Cover Memo	Consider	Paper	
	9.2	IPSASB CP <i>Accounting for Revenue and Non-Exchange Expenses</i>	Note	Paper	
	9.3	IPSASB CP <i>Accounting for Revenue and Non-Exchange Expenses – At a Glance</i>	Note	Paper	
<b>Standards for Noting</b>					
4.15 pm	<b>10</b>	<b><u>Standards Approved</u></b>	(VSF)		
	10.1	Approval 89 NZ IFRIC 23 <i>Uncertainty over Income Tax Treatments</i>	Note	Paper	
	10.2	Approval 90 NZ IFRS 17 <i>Insurance Contracts</i>	Note	Paper	
<b>E: NON-PUBLIC SESSION</b>					
<b>Items for Noting</b>					
4.20 pm	<b>11</b>	<b><u>International &amp; Domestic Update</u></b>			
4.50 pm		<i>Finish</i>			

Forthcoming NZASB meetings:

- Friday 6 October 2017 9am–12pm (via videoconference and teleconference) to discuss IPSASB CP *Accounting Revenue and Non-Exchange Expenses*
- Wednesday 1 November 2017



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## Memorandum

**Date:** 1 September 2017

**To:** NZASB Members

**From:** Lay Wee Ng and Vanessa Sealy-Fisher

**Subject:** Amendments to XRB A1

### Recommendation

1. We recommend that the Board APPROVES *2017 Amendments to XRB A1* to be tabled at the October XRB Board meeting for approval to issue.

### Background

2. Exposure Draft *2017 Amendments to XRB A1* (the ED) was issued in June 2017 by the XRB Board with comments due by 28 August 2017.
3. As explained below, the ED proposed to delete paragraph 9(c) and add paragraph 42A.

#### ***Paragraph 9(c)***

4. Paragraph 9(c) deems an entity to have public accountability if section 55 of the Financial Reporting Act 2013 (FRA 2013) applies. Section 55 contains transitional provisions for the Financial Reporting Act 1993 to continue to apply until 5 years after the commencement of the FRA 2013. That 5-year period ends on 30 November 2017.

#### ***Paragraph 42A***

5. Paragraph 42A requires a public benefit entity (PBE) to determine its eligibility to report in accordance with Tier 4 PBE Accounting Requirements based on the total combined operating payments of the entity and any entities that it controls (that is, on a group basis), which is consistent with the manner in which the size criteria for Tier 1, Tier 2 and Tier 3 PBE Accounting Requirements are determined.
6. This means that where the total operating payments of the group are more than \$125,000 in each of the two preceding accounting periods, the controlling entity would be required to prepare consolidated financial statements using the appropriate tier of financial reporting requirements (Tier 1, Tier 2 or Tier 3).
7. However, where the total operating payments of the group are less than \$125,000 in each of the two preceding accounting periods, all the entities would be eligible to report under Tier 4 PBE Accounting Requirements and the controlling entity would not be required to prepare consolidated financial statements.



8. We have received no formal comment letters. However, we have received an informal email which expressed support for the proposals in the ED (see agenda item 2.3.8).

**Due process**

9. The due process followed by the NZASB complied with the due process requirements established by the XRB Board and, in our view, meets the requirements of section 22 of the Financial Reporting Act 2013.
10. In accordance with section 22(2) of the Financial Reporting Act 2013 we have considered whether the amending standard is likely to require the disclosure of personal information. In our view the amending standard does not include requirements that would result in the disclosure of personal information, and therefore no consultation with the Privacy Commissioner is required.

**Effective date**

11. The amendments are effective for reporting periods beginning on or after 1 January 2018, with earlier application of paragraph 42A permitted.

**Next steps**

12. *2017 Amendments to XRB A1* will be tabled for approval to issue at the October XRB Board meeting.

**Attachment**

Agenda item 3.2: *2017 Amendments to XRB A1*



## **2017 Amendments to External Reporting Board Standard A1 Application of the Accounting Standards Framework**

This Standard was issued on [26 October 2017] by the External Reporting Board pursuant to section 12(a) of the Financial Reporting Act 2013.

This Standard is a disallowable instrument for the purposes of the Legislation Act 2012, and pursuant to section 27(1) of the Financial Reporting Act 2013 takes effect on [23 November 2017].

Reporting entities that are subject to this Standard are required to apply the Standard in accordance with the effective date set out in Part C of this Standard.

In finalising this Standard, the External Reporting Board has carried out appropriate consultation in accordance with section 22(1) of the Financial Reporting Act 2013.

This Standard has been issued to amend XRB A1 to reflect a legislative change and to amend the criteria for a public benefit entity to report in accordance with Tier 4 Accounting Requirements.

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## **Part A**

### **Introduction**

This Standard amends External Reporting Board Standard A1 *Application of the Accounting Standards Framework* by:

- (a) deleting paragraph 9(c); and
- (b) adding paragraph 42A to amend the criteria for an entity to report in accordance with Tier 4 PBE Accounting Requirements.

## Amendments to XRB A1

Paragraph 9(c) is deleted (deleted text is struck through) and paragraphs 42A and 75 are added

### Public Accountability

...

- 9 An entity is deemed to have public accountability in New Zealand if:
- (a) it is an FMC reporting entity or a class of FMC reporting entities that is considered to have a “higher level of public accountability” than other FMC reporting entities under section 461K of the Financial Markets Conduct Act 2013 [footnote omitted]; or
  - (b) it is an FMC reporting entity or a class of FMC reporting entities that is considered to have a “higher level of public accountability” by a notice issued by the Financial Markets Authority (FMA) under section 461L(1)(a) of the Financial Markets Conduct Act 2013~~or~~;
  - ~~(c) it is an entity to which section 55 of the Financial Reporting Act 2013 applies.~~

...

### Tier 4 Criteria

- 42 Subject to the requirements on moving between tiers (set out in paragraphs 47 to 72), a PBE may elect to report in accordance with Tier 4 PBE Accounting Requirements if it is permitted by an Act to report in accordance with non-GAAP standards (i.e., the cash basis of accounting) because it does not have public accountability and does not meet the legislative size threshold to be a “specified not-for-profit entity”. [footnote omitted]
- 42A For the purpose of applying the legislative size threshold, where an entity has controlled entities<sup>1</sup>, total operating payments means the combined operating payments of the entity and all its controlled entities.<sup>2</sup> An entity may elect to report in accordance with Tier 4 PBE Accounting Requirements where the combined total operating payments of the entity and all its controlled entities do not exceed the legislative size threshold. Where the combined total operating payments exceed the legislative size threshold, the entity shall apply the criteria for other tiers to determine the appropriate tier for reporting.

...

### D. EFFECTIVE DATE

...

- 75 *2017 Amendments to XRB A1*, issued in **October 2017**, deleted paragraph 9(c) and added paragraph 42A. Those amendments are effective for reporting periods beginning on or after 1 January 2018. Earlier application of paragraph 42A is permitted.

<sup>1</sup> An entity determines whether it controls another entity in accordance with GAAP.

<sup>2</sup> The combined operating payments of the entity and all its controlled entities excludes any payments between the entity and the controlled entities and/or between the controlled entities.

## **Part C**

### **Effective Date**

This Standard is effective for reporting periods beginning on or after 1 January 2018. Earlier application of paragraph 42A is permitted.



NZ ACCOUNTING  
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## Memorandum

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**Date:** 1 September 2017

**To:** NZASB Members

**From:** Vanessa Sealy-Fisher

**Subject:** **Proposed Amendments to Tier 4 PBE Accounting Requirements**

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### Action required

1. The Board is asked to CONSIDER whether we should undertake further work on the two concerns raised by constituents regarding the Tier 4 not-for-profit standard.

### Background

2. At its meeting in March 2017, the Board noted a letter (see agenda item 2.12) which outlined the impacts of registered charities reporting in accordance with the Tier 4 standard when they control other entities that have significant resources. The letter noted that, if the controlling entity reports in accordance with the Tier 4 standard, it is not required to prepare consolidated financial statements.
3. The letter also noted that although the Tier 4 standard contains requirements for some disclosures about related parties and transactions with related parties, there is no explicit requirement to provide disclosures about controlled/controlling entity relationships (see paragraphs A109–A114 in the Appendix to this memo).
4. Following consideration of the issues raised by the constituent the XRB proposed some amendments to the tier criteria in XRB A1 *Application of the Accounting Standards Framework*. These amendments are expected to be approved by the XRB in the near future (see agenda items 3.1 and 3.2).
5. The informal email which expressed support for the proposed amendments to XRB A1 (see agenda item 2.3.8) noted that the Tier 4 standard contains no explicit requirement for the preparation of consolidated financial statements, nor is there any guidance on how Tier 4 entities should account for their interests in other entities. However, the Tier 3 standard does provide requirements for the preparation of consolidated financial statements and guidance on the accounting for interests in other entities. The constituent queried whether requirements and guidance should be added to the Tier 4 standard.

### Preparation of consolidated financial statements by Tier 4 entities

6. The Tier 4 standard requires the preparation of a performance report with the financial information prepared on a cash basis.



7. In response to the concern raised in agenda item 2.3.9 regarding the preparation of consolidated financial statements by Tier 4 entities, paragraph 42A is to be added to XRB A1 *Application of the Accounting Standards Framework*.

#### **Tier 4 Criteria**

42 Subject to the requirements on moving between tiers (set out in paragraphs 47 to 72), a PBE may elect to report in accordance with Tier 4 PBE Accounting Requirements if it is permitted by an Act to report in accordance with non-GAAP standards (i.e., the cash basis of accounting) because it does not have public accountability and does not meet the legislative size threshold to be a “specified not-for-profit entity”. [footnote omitted]

42A For the purpose of applying the legislative size threshold, where an entity has controlled entities<sup>1</sup>, total operating payments means the combined operating payments of the entity and all its controlled entities.<sup>2</sup> An entity may elect to report in accordance with Tier 4 PBE Accounting Requirements where the combined total operating payments of the entity and all its controlled entities do not exceed the legislative size threshold. Where the combined total operating payments exceed the legislative size threshold, the entity shall apply the criteria for other tiers to determine the appropriate tier for reporting.

<sup>1</sup> An entity determines whether it controls another entity in accordance with GAAP.

<sup>2</sup> The combined operating payments of the entity and all its controlled entities excludes any payments between the entity and the controlled entities and/or between the controlled entities.

8. Paragraph 42A requires a public benefit entity (PBE) to determine its eligibility to report in accordance with the Tier 4 standard based on the total combined operating payments of the entity and any entities that it controls (that is, on a group basis), which is consistent with the manner in which the size criteria for Tier 1, Tier 2 and Tier 3 PBE Accounting Requirements are determined.
9. This means that where the total operating payments of the group are more than \$125,000 in each of the two preceding accounting periods, the controlling entity would be required to prepare consolidated financial statements using the appropriate tier of financial reporting requirements (Tier 1, Tier 2 or Tier 3).
10. However, where the total operating payments of the group are less than \$125,000 in each of the two preceding accounting periods, all the entities would be eligible to report under the Tier 4 standard and the controlling entity would not be required to prepare consolidated financial statements.
11. Agenda item 2.3.8 notes that the Tier 4 standard contains no requirement or guidance for the preparation of consolidated financial statements. As outlined in paragraph 9 above, if a Tier 4 entity controls another entity and the ‘group’ is eligible to report in accordance with the Tier 4 standard, the controlling entity would not be required to prepare consolidated financial statements.

#### **Disclosures about controlled/controlling entity relationships**

12. The Tier 4 standard requires disclosures about related party transactions (paragraph A113) where a person or another entity has significant influence over the entity. Where there are transactions between related parties, the entity is also required to disclose the nature of the related party relationship (paragraph A114).

13. As outlined earlier in this memo, where a Tier 4 entity controls another entity but the total combined operating payments of all the entities in the group are less than \$125,000 all the entities would be eligible to report in accordance with the Tier 4 standard.
14. Where a Tier 4 entity controls another Tier 4 entity and both entities report in accordance with the Tier 4 standard, no disclosures would be made of transactions (and the relationship) between the two entities because the explanation of related parties in the Tier 4 standard refers only to significant influence and not to control.

#### **Recommendation**

15. We recommend that the Board AGREES that we should undertake further work on whether amendments are needed to the Tier 4 standard to:
  - (a) clarify that where an entity controls another entity and both entities qualify to report in accordance with the Tier 4 standard, the controlling entity is not required to prepare consolidated financial statements; and
  - (b) require disclosure of transactions (and the relationship) between controlled and controlling entities that qualify to report in accordance with the Tier 4 standard.

#### **Next steps**

16. If the Board agrees that further work is required, we will table any proposed amendments to the Tier 4 standards at a future meeting together with proposed amendments in respect of implementation issues previously discussed by the Board in May 2017 (agenda item 6).
17. Proposed amendments to the Tier 3 and Tier 4 standards are scheduled for consideration at the December Board meeting.
18. If amendments are made to the Tier 4 not-for-profit standard to address the concerns outlined above, we would also consider making the same amendments to the Tier 4 public sector standard.

#### **Attachments**

- Agenda item 2.3.8: Email from constituent regarding guidance about consolidated financial statements in the Tier 4 standard
- Agenda item 2.12: Letter from constituent regarding Tier 4 controlling entities



NZ ACCOUNTING  
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## Memorandum

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**Date:** 1 September 2017

**To:** NZASB Members

**From:** Lisa Kelsey and Dave Bassett

**Subject:** IASB Disclosure Initiative—Principles of Disclosure

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### Action required<sup>1</sup>

1. The Board is asked to:
  - (a) CONSIDER the submission received on the *Principles of Disclosure* Discussion Paper (the DP);
  - (b) NOTE the feedback received from the Corporate Reporting Users' Forum (CRUF) (Appendix A); and
  - (c) APPROVE the comment letter to the IASB on the DP (agenda item 4.2).

### Background

2. At its August 2017 meeting, the Board considered a draft comment letter on the DP in bullet point format to the IASB. The Board provided feedback on the staff's preliminary response to the fifteen questions for respondents contained in the DP.
3. On the 3 August 2017, we attended the CRUF<sup>2</sup> meeting as observers. The AASB staff had provided the CRUF members with some presentation slides on the DP. The slides focused on the following four areas: cross-referencing, performance measures in the financial statements, unusual or infrequently occurring items and other issues. The AASB staff have compiled a summary of feedback received at the forum and we have included this at Appendix A.
4. The comment period to the NZASB on the DP closed on 18 August 2017. We have received one submission. The comment period to the IASB closes on the 2 October 2017, we are therefore seeking approval of an NZASB comment letter at this meeting.

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<sup>1</sup> This memo refers to the work of the International Accounting Standards Board (IASB) and uses registered trademarks of the IFRS Foundation (for example, IFRS® Standards, IFRIC® Interpretations and IASB® papers).

<sup>2</sup> The CRUF was set up in 2005 by users of financial reports for users of financial reports to be an open forum for learning about and responding to the many accounting and regulatory changes that affect corporate reporting. CRUF participants include buy and sell-side analysts, credit ratings analysts, fund managers and corporate governance professionals.

### Structure of this memo

5. The remaining sections in this memo are set out as follows.

- (a) Submission received;
- (b) Comment letter to the IASB;
- (c) Recommendations; and
- (d) Next steps.

### Submission received

6. The submission received on the DP is set out in Table 1 below.

**Table 1 Submissions received**

Respondent #	Respondent name
R1	Bill Jamieson FCA (copy of submission in supporting papers agenda item 4.3)

7. R1 also commented directly to the IASB. R1's interest is the primary financial statements. R1 supported the view expressed by the IASB in the DP, which is that many readers pay more attention to the primary financial statements than to the rest of the annual accounts. We have read R1's recently published book *"The Accounting Jungle and How to Find Your Way Through it"*. In the book R1 acknowledges that the increasing complexity and length of accounting statements has led to a general demand for financial information to be presented in a form that readers can understand (particularly smaller retail investors). The book discusses each of the primary financial statements in turn to arrive at the key information in them, and the best format to convey that information. The IASB has a current research project — *Primary Financial Statements* examining potential targeted improvements to the structure and content of the primary financial statements with a particular focus on the statement(s) of financial performance and the statement of cash flows. We believe R1's book is more relevant to that project.
8. CA ANZ have advised us that they will submit directly to the IASB. They are in the process of preparing a joint submission with the Association of Chartered Certified Accountants (ACCA).

### Comment letter to IASB

9. The comment letter (agenda item 4.2) incorporates feedback received from the Board, at its August 2017 meeting, on the staff's preliminary response to the questions contained in the DP.

### **Recommendations**

10. We recommend that the Board:

- (a) CONSIDER the submission received on the DP;
- (b) NOTE the feedback received from the CRUF (Appendix A); and
- (c) APPROVE the comment letter to the IASB on the DP (agenda item 4.2).

### **Next steps**

11. As comments to the IASB close on the 2 October 2017, we would request that any changes to the comment letter agreed at this meeting are signed off by the Chair.

### **Attachments**

Agenda item 4.2: Draft comment letter to the IASB

Agenda item 4.3: Submission received — Bill Jamieson

## APPENDIX A

### CRUF Meeting Summary: Making Disclosures more relevant and concise (August 2017)

Topic / Question	Feedback
1. Should entities be allowed to provide information necessary to comply with IFRS outside the financial statements, but within the annual report?	<ul style="list-style-type: none"> <li>• Cross-referencing could lead to entities “hiding” unfavourable disclosures, by making them harder to find (i.e. onus on users to follow through).</li> <li>• These days with most users reading financial statements via web access, even if they are long, users can just click (navigate) into the sections that they want to read. Therefore, there is less of a need for cross-referencing to IFRS information outside the financial statements.</li> <li>• It was noted that approx. 10% of investors (retail) still want access to hardcopy annual report, so arguably for those investors the annual report would need to be a standalone document.</li> <li>• It was noted that the ASX’s <i>Principles of Good Corporate Governance and Good Practice Recommendations</i> allow cross-referencing to governance and policy documents via hyperlink to the entity’s website, most companies are now making use of this and users find this helpful. Therefore, where used appropriately, cross-referencing to information outside the financial statements could be helpful.</li> <li>• Some participants supported making sections, such as the Remuneration Report available via cross-link to a website.</li> </ul>
2. Should all performance measures have the following requirements: <ol style="list-style-type: none"> <li>a) Have no more prominence than IFRS</li> <li>b) Reconcile to IFRS</li> <li>c) Be explained why relevant in notes to Financial Statements</li> <li>d) Be neutral, free from error, clearly labelled</li> <li>e) Contain comparatives</li> <li>f) Classified, measured and presented consistently</li> <li>g) Be clear whether they have been audited or not?</li> </ol>	<ul style="list-style-type: none"> <li>• Most participants agreed that Performance Measures can be useful and the IASB’s proposed requirements for fair presentation, which are largely consistent with requirements in RG230 <i>Disclosing non-IFRS financial information</i>, appear reasonable. As such, there was support for the approach suggested by the IASB.</li> <li>• The AASB noted that ASIC would need to reconsider guidance if the IASB changed its requirements.</li> <li>• It was noted that one of the reasons users find Performance Measures useful, is because they provide insight into Management decision making and focus.</li> <li>• Participants didn’t object to having Performance Measures on the “Face” of the financial statements as long as they are reconcilable to IFRS.</li> <li>• It was suggested that there could be a designated section in the financial statements for reconciliations of all Performance Measures to IFRS. That way, when Performance Measures are used they could be accompanied by a reference to this section.</li> <li>• It was noted that Performance Measures are not usually contained in the financial statements in Australia (because of RG230) but participants from New Zealand noted that IFRS did not prohibit the presentation of Performance Measures (as long as they are no more prominent than IFRS). The guidance produced by the regulator in NZ (FMA) is for Performance Measures presented outside the financial statements.</li> <li>• It was also noted that Performance Measures are generally not audited in Australia (because outside of financial statements). Although one participant did suggest that if a Performance Measure simply added components of audited IFRS, then arguably that Performance Measure has been audited.</li> <li>• It was suggested that there should be a further discussion on EBIT/EBITDA. The AASB noted that this is being considered as part of the IASB’s <i>Primary Financial Statements</i> Project and this was also discussed at the last ASAF meeting.</li> </ul>
3. Should we have definitions of, and requirements for, the presentation of unusual or infrequently occurring items?	<ul style="list-style-type: none"> <li>• Participants acknowledged the difficulty in defining these terms. Emphasis should be on developing principles for the presentation of these items. Users need insights into why management has made adjustments, users may take a different approach and make different decisions on how to treat these items, but the key is that users are given sufficient information to make informed decisions.</li> <li>• It was noted that generally non-recurring items tend to be expenses and not revenue and this should be addressed as part of this issue (i.e. entities should not be allowed to cherry pick the adjustments they make).</li> <li>• It was also noted that entities seem to disclose “recurring” non-recurring items (suggesting that they aren’t really non-recurring).</li> <li>• It was acknowledged that if these items were permitted, that auditing them would be challenging (e.g. difficulties in determining what is truly “infrequent” and ensuring entities adjust for infrequent revenue and not just expenses).</li> </ul>
4. Other comments	<ul style="list-style-type: none"> <li>• CRUF are engaging with the IASB in September and will cover this topic.</li> <li>• It was also suggested to get Doug Niven in to discuss ASIC’s view (including discussion over NZ differences).</li> </ul>



NZ ACCOUNTING  
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2 October 2017

Mr Hans Hoogervorst  
Chairman of the International Accounting Standards Board  
IFRS Foundation  
30 Cannon Street  
London EC4M 6XH  
**United Kingdom**

Submitted to: [www.ifrs.org](http://www.ifrs.org) or By email: [commentletters@ifrs.org](mailto:commentletters@ifrs.org)

Dear Hans

#### **DP/2017/1 Disclosure Initiative–Principles of Disclosure**

Thank you for the opportunity to comment on DP/2017/1 *Disclosure Initiative–Principles of Disclosure* (the DP). The DP has been exposed in New Zealand and some New Zealand constituents may have made comments directly to you.

We are very supportive of the IASB's focus on the theme of Better Communication and its *Disclosure Initiative*. We believe that there is a need to improve the communication effectiveness of financial statement disclosures, and are therefore supportive of the objective of the *Principles of Disclosure* project.

We conducted a range of outreach activities, including workshops in several cities across New Zealand. We are grateful for the assistance of the IASB staff in providing a presentation of the DP at those workshops. NZASB staff have collated feedback from our outreach activities and have shared this with IASB staff.

As an international standard setter, the IASB plays an important role in improving the disclosure effectiveness of financial statements. However, we acknowledge that other financial statement stakeholders also have an important part to play in overcoming the disclosure problem.

Many New Zealand entities have already taken steps in the last few years to improve the disclosure effectiveness of their financial statements. The improvements have included providing more entity-specific disclosures, avoiding boilerplate language, re-ordering disclosures and removing disclosures considered irrelevant or immaterial. Often entities have worked with their auditors to achieve these improvements in their financial statements.

Locally, the New Zealand Financial Markets Authority<sup>1</sup> (FMA) is playing an active role in trying to improve financial statements as a clear and effective reporting and communication tool. The FMA hosted a discussion forum in September 2014 to bring together financial statement stakeholders to understand and discuss the disclosure challenges within the New Zealand environment. The FMA has been vocal in its belief that the disclosure of clear, concise and effective financial information provides investors with access to information that will help them make informed financial decisions.

Looking to the future, we believe that the IASB needs to give more consideration to how financial information will be consumed by users in the next decade and beyond. The rise of digital reporting and interactive financial statements may present other opportunities to address the “disclosure problem”. Currently financial statements are thought of as a hard copy document or a downloadable PDF. Digital reports will be much more interactive documents, that will allow for enhanced searchability, enabling analysts to drill down to obtain further information and retail investors to obtain the information they need at a summarised level. At a minimum, we believe that the IASB should seek to further explore/develop disclosure principles for financial statements made available in digital format.

Our recommendations and responses to the specific questions for respondents are provided in the Appendix to this letter. If you have any queries or require clarification of any matters in this letter, please contact David Bassett ([David.Bassett@xrb.govt.nz](mailto:David.Bassett@xrb.govt.nz)), Lisa Kelsey ([Lisa.Kelsey@xrb.govt.nz](mailto:Lisa.Kelsey@xrb.govt.nz)) or me.

Yours sincerely

Kimberley Crook  
**Chair – New Zealand Accounting Standards Board**

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<sup>1</sup> The FMA is one of three main regulators in New Zealand. The FMA regulates capital markets and financial services in New Zealand.



# Appendix to Principles of Disclosure Discussion Paper comment letter to IASB

## Section 1—Overview of the “disclosure problem” and the objective of this project

Question 1
<p>Paragraphs 1.5–1.8 describe the disclosure problem and provide an explanation of its causes.</p> <p>(a) Do you agree with this description of the disclosure problem and its causes? Why or why not? Do you think there are other factors contributing to the disclosure problem?</p> <p>(b) Do you agree that the development of disclosure principles in a general disclosure standard (i.e. either in amendments to IAS 1 or in a new general disclosure standard) would address the disclosure problem? Why or why not?</p>

### Question 1(a)

We agree with the description of the “disclosure problem” and its causes in the DP.

The IASB’s description of the disclosure problem and its causes are largely consistent with the findings from the New Zealand Financial Markets Authority’s (FMA) discussion forum titled “Beyond International Financial Reporting Standards (IFRS): Quality Financial Reporting”. The discussion forum was held in September 2014 and attended by financial reporting preparers, users, standard setters, auditors, lawyers and regulators. The forum aimed to facilitate a clearer understanding of disclosure challenges within the New Zealand environment, and identify ways to improve financial statements so they are a clear and effective reporting and communication tool.

The FMA produced a summary of the main findings from the forum: *Quality Financial Reporting – How to Improve Financial Statements*<sup>2</sup> (FMA report). These findings included the following.

- (a) Some financial statements contain content that is not relevant or material, potentially obscuring the information that is important.
- (b) Financial statements that are not clear, concise and effective have an adverse impact on the effective communication channels between entities and their users.
- (c) Application of the concept of materiality in practice is seen by many as a major cause of disclosure overload. This may be due to a failure to use managements’ professional judgement when considering materiality.
- (d) The reasons for disclosure overload are linked to the behavioural patterns of financial statement stakeholders (preparers, directors, auditors, standard setters and regulators).

<sup>2</sup> <https://fma.govt.nz/assets/Reports/141101-Quality-Financial-Reporting-How-To-Improve-Financial-Statements2014.pdf>

*Question 1(b)*

We agree that the development of disclosure principles in a general disclosure standard would help towards addressing the disclosure problem.

In our view, the development of disclosure principles would improve the effectiveness of disclosures for users of financial statements by:

- (a) providing preparers with guidance on how to disclose and communicate information effectively;
- (b) giving preparers confidence to apply judgement in deciding what information to disclose and how to disclose information; and
- (c) helping the IASB improve disclosure requirements.

Although we consider that (a) and (c) have a role in addressing the disclosure problem, we believe that (b) may play a greater role in addressing the disclosure problem. In our view behavioural issues in applying judgement play a larger part in contributing to the disclosure problem, compared to a lack of guidance or existing requirements in IFRS Standards.

This view is consistent with steps taken, over the past couple of years, by many New Zealand entities to improve the disclosure effectiveness of their financial statements. These improvements which included re-ordering disclosures, providing more entity-specific disclosures, avoiding boilerplate language and removing disclosures considered irrelevant or immaterial, were achieved under existing requirements in IFRS Standards.

Consistent with feedback received by the IASB, we believe that behavioural issues extend beyond preparers, and include a number of different stakeholders (including regulators and auditors), who all have a role to play in addressing the disclosure problem. We believe that the development of disclosure principles will play a role in driving a positive shift in stakeholder perceptions of financial statements. Stakeholders that view financial statements as a compliance document, rather than a means of communication, may contribute to the disclosure problem by imposing “limitations” on a preparers’ ability to apply judgement (e.g. the strict use of disclosure checklists by an auditor). A shift in stakeholder perceptions towards viewing financial statements as a means for communication would hopefully help to reduce the extent of those imposed limitations and ultimately increase the confidence of preparers to apply judgement.

**Question 2**

Sections 2–7 discuss specific disclosure issues that have been identified by the IASB and provide the IASB’s preliminary views on how to address these issues.

Are there any other disclosure issues that the IASB has not identified in this Discussion Paper that you think should be addressed as part of this Principles of Disclosure project? What are they and why do you think they should be addressed?

*Materiality*

The FMA identified in its report *Quality Financial Reporting – How to Improve Financial Statements*<sup>3</sup> that materiality is well-established as a concept in relation to recognition and measurement, but not so much when it comes to disclosures. We believe that this signals a need for specific guidance on making judgements on materiality in relation to disclosures.

We acknowledge that within the *Disclosure Initiative* there are two other projects, namely the *Definition of Materiality* and *Materiality Practice Statement* projects. These projects will be key in helping support changes in stakeholder behaviour towards applying materiality in relation to disclosures.

*Digital reporting*

We believe that the IASB needs to give more consideration to how financial information will be consumed by users in the future. The rise of digital reporting and interactive financial statements may present other opportunities to address the “disclosure problem”. Currently financial statements are thought of as a hard copy document or a downloadable PDF. Digital reports will be much more interactive documents, that will allow for enhanced searchability, enabling analysts to drill down to obtain further information and retail investors to obtain the information they need at a summarised level. At a minimum, we believe that the IASB should seek to further explore/develop disclosure principles for financial statements made available in digital format. Also see the related point below.

*CORE & MORE*

In 2015, Accountancy Europe (previously Federation of European Accountants) published *The Future of Corporate Reporting – creating the dynamic for change*<sup>4</sup>. The paper sets out a possible way of presenting and linking information to be reported, through the CORE & MORE concept: a CORE report provides an overview of corporate affairs accompanied by MORE report(s) which provide detailed information complementing the CORE report.

We consider that there is merit in the IASB exploring the development of such a presentation approach to financial reporting. We believe that such an approach could be given life through digital reporting, which through the use of hyperlinks could enable users to drill-down (access) detailed information contained in the MORE report(s) from the CORE report.

<sup>3</sup> See footnote 2.

<sup>4</sup> [https://www.accountancyeurope.eu/wp-content/uploads/FEECogitoPaper - FutureofCorporateReporting.pdf](https://www.accountancyeurope.eu/wp-content/uploads/FEECogitoPaper_-_FutureofCorporateReporting.pdf)

## Section 2—Principles of effective communication

### Question 3

The IASB's preliminary view is that a set of principles of effective communication that entities should apply when preparing the financial statements as described in paragraph 2.6 should be developed. The IASB has not reached a view on whether the principles of effective communication should be prescribed in a general disclosure standard or described in non-mandatory guidance.

The IASB is also of the preliminary view that it should develop non-mandatory guidance on the use of formatting in the financial statements that builds on the guidance outlined in paragraphs 2.20–2.22.

- (a) Do you agree that the IASB should develop principles of effective communication that entities should apply when preparing the financial statements? Why or why not?
- (b) Do you agree with the principles listed in paragraph 2.6? Why or why not? If not, what alternative(s) do you suggest, and why?
- (c) Do you think that principles of effective communication that entities should apply when preparing the financial statements should be prescribed in a general disclosure standard or issued as non-mandatory guidance?
- (d) Do you think that non-mandatory guidance on the use of formatting in the financial statements should be developed? Why or why not?

If you support the issuance of non-mandatory guidance in Question 3(c) and/or (d), please specify the form of non-mandatory guidance you suggest (see paragraph 2.13(a)–(c)) and give your reasoning.

### Question 3(a)

We agree that the IASB should develop principles of effective communication that entities should apply when preparing the financial statements.

While we believe that the principles are largely common sense, we think that it is beneficial for the IASB to clearly identify and describe communication principles to assist entities when preparing financial statements.

We believe that communication principles will help to improve the communication effectiveness of financial statements by (i) providing preparers with useful guidance on how to communicate effectively; and (ii) encouraging preparers to apply judgement in determining what information to disclose and how to disclose information effectively.

### Question 3(b)

We agree with the principles of effective communication listed in paragraph 2.6 of the DP. The principles are broadly consistent with the principles identified by the FMA in its report *Quality Financial Reporting – How to Improve Financial Statements*.<sup>5</sup>

However, we recommend that the IASB explores combining/condensing the seven principles into three or four principles, to make the principles more workable in practice. Our recommendation is

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<sup>5</sup> See footnote 2.

consistent with feedback received during the Asian-Oceanian Standard-Setters Group 2016 Annual conference held in Wellington, New Zealand.

We consider that the relevance of information and concept of materiality play a central role in improving communication effectiveness. We note that *relevance* is a fundamental qualitative characteristic in the IASB's *Conceptual Framework* and *materiality*, is an entity-specific aspect of *relevance*. While it would be inappropriate for the IASB to consider relevance and materiality as communication principles, we believe that it would be appropriate for the IASB to increase their visibility by including a discussion of *relevance* and *materiality* to accompany the principles of effective communication.

#### *Question 3(c)*

We think that principles of effective communication should be issued as non-mandatory guidance. Given the inter-relationship between some of the principles and the potential need for an entity to make a trade-off between some of the principles of effective communication, e.g. entity-specific information vs comparable information, we do not consider that issuing the principles as mandatory requirements would be suitable. This view is further supported by concerns heard from New Zealand constituents regarding potential difficulties in auditing and enforcing the principles, should they be mandatory requirements.

In our view, the principles should be included in guidance that accompanies, but does not form part of, a general disclosure standard, rather than as a practice statement or educational material. This would have the benefits of: (i) having greater visibility than other forms of non-mandatory guidance such as a practice statement or educational material; and (ii) being subject to the IASB's full due process.

#### *Question 3(d)*

We support the development of non-mandatory guidance on the use of formatting in the financial statements. We think that such formatting guidance should accompany the principles of effective communication, in the form of illustrative examples or implementation guidance that accompany, but do not form part of, the general disclosure standard.

Whilst the DP acknowledges digital reporting and that much of the proposed guidance on the use of formatting is equally applicable to digital reporting, we believe that the proposed guidance could go further in providing formatting guidance for digital reports, e.g. the use of hyperlinks within a set of financial statements.

### Section 3—Roles of the primary financial statements and the notes

#### Question 4

The IASB's preliminary views are that a general disclosure standard should:

- specify that the “primary financial statements” are the statements of financial position, financial performance, changes in equity and cash flows;
- describe the role of primary financial statements and the implications of that role as set out in paragraphs 3.22 and 3.24;
- describe the role of the notes as set out in paragraph 3.28, as well as provide examples of further explanatory and supplementary information, as referred to in paragraphs 3.26–3.27; and
- include the guidance on the content of the notes proposed in paragraphs 7.3–7.7 of the *Conceptual Framework* Exposure Draft, as described in paragraph 3.7.

In addition, the IASB's preliminary views are that:

- it should not prescribe the meaning of “present” as presented in the primary financial statements and the meaning of “disclose” as disclosed in the notes; and
- if it uses the terms “present” and “disclose” when describing where to provide information in the financial statements when subsequently drafting IFRS Standards, it should also specify the intended location as either “in the primary financial statements” or “in the notes”.

Do you agree with the IASB's preliminary views? Why or why not? If you do not agree, what do you suggest instead, and why?

*Specify that the “primary financial statements” are the statements of financial position, financial performance, changes in equity and cash flows*

While our preference would be for the IASB and the International Public Sector Accounting Standards Board (IPSASB) to align terms, we do not have concerns with the use of the term “primary financial statements” and note that this term is generally well understood in practice.<sup>6</sup>

In general, we agree with the view that the “primary financial statements” are the statement of financial position, statement(s) of profit or loss and other comprehensive income, statement of changes in equity and statement of cash flows. However, we suggest that the IASB acknowledges that there may be cases where other statements will be relevant, e.g. entities reporting under IAS 26 *Accounting and Reporting by Retirement Benefit Plans* could produce a statement of net assets available for benefits and a statement of changes in net assets available for benefits.

*Describe the role of primary financial statements and the implications of that role as set out in paragraphs 3.22 and 3.24*

#### Role

We agree that a general disclosure standard should describe the roles of the different components of the financial statements and how those roles meet the objective of financial statements – for the reasons described in paragraph 3.21 and 3.25 of the DP. However, we believe that further work is needed to ensure that the description of the role of the primary financial statements and the

<sup>6</sup> The IPSASB uses the term “face of the financial statements” in its *Conceptual Framework*.

description of the role of the notes together meet the objective of financial statements described in the IASB's *Conceptual Framework Exposure Draft*.

The proposed role of the primary financial statements is inconsistent with the objective of financial statements which references "assessing the prospects for future net cash inflows to the entity and in assessing management's stewardship of the entity's resources". The IASB's preliminary view is that the statement of cash flows is one of the primary financial statements, yet the role of the primary financial statements does not reflect this.

### Implications

We agree with the implications of the role of the primary financial statements described in paragraph 3.24 of the DP.

The IASB's preliminary view in paragraph 3.24(a) of the DP, that information in the "primary financial statements" is more prominent than information in the notes, is consistent with feedback received from New Zealand constituents – which is that many readers pay more attention to the primary financial statements than to the rest of the financial statements.

Paragraph 3.24(e) states that "a decision on whether to present information as a separate line item in the primary financial statements is made after considering the role of the primary financial statements". We suggest that the IASB also acknowledges in paragraph 3.24(e) that materiality plays a role when deciding whether to present information as a separate line item in the primary financial statements.

*Describe the role of the notes as set out in paragraph 3.28, as well as provide examples of further explanatory and supplementary information, as referred to in paragraphs 3.26–3.27*

We agree that the role of the notes to the financial statements should be included in a general disclosure standard with further explanatory and supplementary information.

We echo comments made in the EFRAG *Preliminary response to the questions in the IASB Discussion Paper DP/2017/1 Disclosure Initiative – Principles of Disclosure* that the statement of cash flows and the statement of changes in equity also provide forms of reconciliation and therefore this cannot be seen as a discriminating factor when describing the role of the notes.

We recommend that the IASB considers amending paragraph 3.28(a) as follows.

The role of the notes is to:

- (a) provide further information necessary to disaggregate, ~~reconcile~~ and explain the items recognised in the primary financial statements; and
- (b) ...

*Include the guidance on the content of the notes proposed in paragraphs 7.3–7.7 of the Conceptual Framework Exposure Draft, as described in paragraph 3.7*

We do not have any concerns with the proposed paragraphs 7.3–7.7 of the *Conceptual Framework Exposure Draft* being included in a general disclosure standard.

*It should not prescribe the meaning of “present” as presented in the primary financial statements and the meaning of “disclose” as disclosed in the notes. If it uses the terms “present” and “disclose” when describing where to provide information in the financial statements when subsequently drafting IFRS Standards, it should also specify the intended location as either “in the primary financial statements” or “in the notes”.*

We support the IASB’s proposal to specify the intended location if it uses the terms “present” or “disclose”. We believe that specifying the intended location is more important than defining the terms “present” and “disclose”.<sup>7</sup> We also believe that this will help to address confusion regarding the location of information when “present” and “disclose” are used.

However, we have concerns that more prescriptive wording of “present in the primary financial statements” could have the unintended consequence of being misinterpreted as a requirement that is not subject to materiality. This concern could be addressed by giving greater emphasis to materiality when drafting disclosure requirements, e.g. by including a paragraph in each standard reminding entities to apply materiality, see the “Guidance on the use of judgement” paragraphs in the NZASB staff’s example in section 8 of the DP as a starting point.

While we do not believe that the IASB should formally prescribe a meaning for “present” and “disclose”, we do think the terms should be used consistently.

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<sup>7</sup> We note that the IPSASB in its Conceptual Framework uses the term “display” for the face of the financial statements and “disclose” for the notes of the financial statements.



**Section 4—Location of information****Question 5**

The IASB's preliminary view is that a general disclosure standard should include a principle that an entity can provide information that is necessary to comply with IFRS Standards outside financial statements if the information meets the requirements in paragraphs 4.9(a)–(c).

- (a) Do you agree with the IASB's preliminary view? Why or why not? If you do not agree, what alternative(s) do you suggest, and why?
- (b) Can you provide any examples of specific scenarios, other than those currently included in IFRS Standards (see paragraphs 4.3–4.4), for which you think an entity should or should not be able to provide information necessary to comply with IFRS Standards outside the financial statements? Why? Would those scenarios meet the criteria in paragraphs 4.9(a)–(c)?

**Question 5(a)**

We agree that a general disclosure standard should include a general principle that an entity can provide information that is necessary to comply with IFRS Standards outside of the financial statements provided certain requirements are met.

Permitting cross-referencing to IFRS information outside the financial statements would help to reduce duplication of information within the annual report, shorten disclosures in the financial statements and highlight relationships between pieces of information.

We note that the International Standards on Auditing recognise that explanatory or descriptive information may be included in the financial statements by cross-reference to information in another document, and that information will form part of the financial statements.

**Criteria for cross-referencing (the requirements in paragraphs 4.9(a)–(c))**

We do not agree with the requirement expressed in paragraph 4.9(a) of the DP that limits cross-referencing to within the annual report. The IASB needs to consider how information is expected to be consumed in the future. In our view, cross-referencing needs to be permitted on a wider basis than the annual report. Any cross-referencing requirements should be future-proofed to take into account the continued advancements in digital reporting and the rise of interactive reports (where the boundaries of the annual report and financial statements can become unclear). We also note that section 6—*Disclosure of Accounting Policies* of the DP considers cross-referencing certain accounting policies to an entity's website.

We believe that it would be more appropriate to broaden the requirement in paragraph 4.9(a) of the DP to permit cross-referencing where IFRS information outside of the financial statements is available on the same terms, at the same time and continues to be available as long as the financial statements.

We partly agree with the requirement expressed in paragraph 4.9(b) of the DP that cross-referencing to IFRS information outside the financial statements should be permitted only if the financial statements remain understandable and the information is faithfully represented.

We believe that this requirement will help address concerns raised that cross-referencing could be overused or misused. However, we do not agree with the requirement that “the location of the information makes the annual report as a whole more understandable”. We consider that the understandability of the annual report as a whole is outside of the IASB’s mandate.

We agree with the requirement expressed in paragraph 4.9(c) of the DP that cross-referenced information needs to be clearly identified and should be incorporated in the financial statements by means of a cross-reference to that information that is made in the financial statements. It is vital that cross-referenced information is required to be clearly identified.

We further recommend that the IASB consider requiring that cross-referenced information outside the financial statements must also be clearly identifiable as being audited or not.

#### Question 5(b)

We have heard that there are situations where entities have provided information required by IFRS 8 *Operating Segments* and IAS 24 *Related Party Disclosures* outside of the financial statements but within the annual report. However, we have not found the use of cross-referencing to IFRS information outside of the financial statements to be extensive in New Zealand.

We have not identified any examples of specific scenarios where we think an entity should be prohibited from providing information necessary to comply with IFRS Standards outside the financial statements, provided such information meets certain requirements, as discussed under question 5(a) above.

We are not aware of any statutory or regulatory requirements in New Zealand that would restrict an entity from providing information necessary to comply with IFRS Standards outside the financial statements.

#### Question 6

The IASB’s preliminary view is that a general disclosure standard:

- should not prohibit an entity from including information in its financial statements that it has identified as “non-IFRS information”, or by a similar labelling, to distinguish it from information necessary to comply with IFRS Standards; but
- should include requirements about how an entity provides such information as described in paragraphs 4.38(a)–(c).

Do you agree with the IASB’s preliminary view? Why or why not? If you do not agree, what alternative(s) do you suggest, and why?

*A general disclosure standard should not prohibit an entity from including information in its financial statements that it has identified as “non-IFRS information”, or by a similar labelling, to distinguish it from information necessary to comply with IFRS Standards*

We partially agree with the IASB’s preliminary view, in that we agree that a general disclosure standard should not prohibit an entity from including other information in its financial statements, subject to the points discussed below.

In our view, prohibiting “non-IFRS information” from being disclosed in the financial statements could:

- (a) be challenging to operationalise and could result in useful information being omitted because of the potential difficulty in differentiating between IFRS information in Category B and “non-IFRS information” in Category C;
- (b) have an unintended consequence on the ability for entities to assert compliance with IFRS in jurisdictions like New Zealand that have adopted IFRS Standards, but may also have additional country-specific disclosure requirements, which could be considered “non-IFRS information”; and
- (c) prevent entities from including statutory or regulatory disclosures as part of their audited financial statements.

*A general disclosure standard should include requirements about how an entity provides such information as described in paragraphs 4.38(a)–(c)*

We do not agree with the requirements in paragraph 4.38. We believe that entities should focus on what additional information to include in their financial statements in order to achieve a fair presentation rather than on differentiating between IFRS information and “non-IFRS information”. Additionally, we believe the disclosure requirements in paragraph 4.38 have the potential to increase the clutter in the financial statements.

We would prefer that the IASB develops principles around the fair presentation of “additional” information, e.g. any additional information presented or disclosed in the financial statements, beyond the requirement of IFRS Standards, shall not be misleading or biased.

We note the overlap between “non-IFRS information” and performance measures discussed in Section 5—*Use of performance measures in the financial statements*. When drafting a general disclosure standard, we believe it will be important for the IASB to make clear that if information provided also fits the description of a performance measure, any requirements relating to performance measures would also apply.

#### Question 7

The IASB did not discuss whether any specific information—for example, information that is inconsistent with IFRS Standards—should be required to be identified as described in paragraphs 4.38(a)–(c) or should be prohibited from being included in the financial statements. Do you think the IASB should prohibit the inclusion of any specific types of additional information in the financial statements? If so, which additional information, and why?

We do not think the IASB should prohibit the inclusion of any specific types of additional information in the financial statements as this could prevent an entity from telling its story. However, as we suggested above, the IASB should include principles around the fair presentation of such information, e.g. any additional information presented or disclosed in the financial statements, beyond the requirement of IFRS Standards, shall not be misleading or biased.

**Section 5—Use of performance measures in the financial statements**

**Question 8**

The IASB's preliminary views are that it should:

- clarify that the following subtotals in the statement(s) of financial performance comply with IFRS Standards if such subtotals are presented in accordance with paragraphs 85–85B of IAS 1:
    - the presentation of an EBITDA subtotal if an entity uses the nature of expense method; and
    - the presentation of an EBIT subtotal under both a nature of expense method and a function of expense method.
  - develop definitions of, and requirements for, the presentation of unusual or infrequently occurring items in the statement(s) of financial performance, as described in paragraphs 5.26–5.28.
- (a) Do you agree with the IASB's preliminary views? Why or why not? If you do not agree, what alternative action do you suggest, and why?
- (b) Should the IASB prohibit the use of other terms to describe unusual and infrequently occurring items, for example, those discussed in paragraph 5.27?
- (c) Are there any other issues or requirements that the IASB should consider in addition to those stated in paragraph 5.28 when developing requirements for the presentation of unusual or infrequently occurring items in the statement(s) of financial performance?

The feedback on Question 8 will be considered as part of the IASB's Primary Financial Statements project.

**Question 8(a)**

*The IASB should clarify that the following subtotals in the statement(s) of financial performance comply with IFRS Standards if such subtotals are presented in accordance with paragraphs 85–85B of IAS 1:*

- *the presentation of an EBITDA subtotal if an entity uses the nature of expense method; and*
- *the presentation of an EBIT subtotal under both a nature of expense method and a function of expense method.*

We do not agree that it is necessary for the IASB to clarify when the presentation of EBIT and EBITDA provides a fair presentation. We believe the current requirements in paragraph 85A of IAS 1 are sufficient to ensure entities do not provide subtotals that disrupt the analysis of expenses. We would not expect an entity to provide an EBITDA subtotal when an entity uses the function of expense approach.

An entity may disclose EBITDA adjacent to the statement(s) of financial performance when the function of expenses method is used. If an entity did this we note that it would be subject to the requirements proposed in the DP for the fair presentation of performance measures.

*The IASB should develop definitions of, and requirements for, the presentation of unusual or infrequently occurring items in the statement(s) of financial performance, as described in paragraphs 5.26–5.28.*

We believe it is entity and industry specific as to what is considered unusual or infrequent and it would be extremely difficult for the IASB to define these terms. We therefore do not agree the IASB

should proceed with proposals to develop definitions of, and requirements for, the presentation of unusual or infrequently occurring items. We suggest instead that the IASB develop principles for the fair presentation of these items. We have discussed this further in our response to question 8(c) below.

*Question 8(b)*

We do not believe that the IASB should prohibit the use of other terms to describe unusual and infrequently occurring items. Rather than focusing on the terms used, for which there could be many alternative terms, we suggest that the IASB establishes requirements for the fair presentation of these items. We have discussed this further in our response to question 8(c) below.

*Question 8(c)*

We acknowledge that information on unusual or infrequently occurring items is useful to users of financial statements, because it helps them to assess the recurring/sustainable performance and make assessments about the future, provided the items are genuinely unusual or infrequently occurring. We received feedback that sometimes entities only adjusted for those unusual or infrequently occurring items that had a negative effect on performance and did not adjust for those that had a positive effect. Users need insight into why management has made the adjustments – this will allow users to make informed decisions about these adjustments.

We suggest that the IASB, rather than focusing on the terms used, should establish requirements for the fair presentation of these items. These requirements at a minimum should require an explanation of why the item is considered unusual or infrequently occurring and require entities to ensure consistency around the use of these terms.

We note that unusual or infrequently occurring items are often used to derive performance measures, therefore we think that the fair presentation requirements for the use of unusual or infrequently occurring items should be a subset of the fair presentation requirements for performance measures in section 5 of the DP. This would avoid entities having to make somewhat repetitive disclosures.

**Question 9**

The IASB's preliminary view is that a general disclosure standard should describe how performance measures can be fairly presented in financial statements, as described in paragraph 5.34. Do you agree with the IASB's preliminary view? Why or why not? If you do not agree, what alternative action do you suggest, and why?

We agree with the IASB's preliminary view that a general disclosure standard should describe how performance measures can be fairly presented in financial statements, as described in paragraph 5.34. We note the XRB undertook a survey to better understand how APMs are viewed and whether APMs are effective in meeting the needs of users of financial reports in New Zealand.<sup>8</sup> Results of the survey were published by the XRB in July 2017, and we have attached to this submission a copy of both the summary of the survey and the full report. The survey supports the

<sup>8</sup> <https://www.xrb.govt.nz/dmsdocument/2317>

views expressed by the IASB in the DP that most users have said that performance measures presented in, or disclosed adjacent to, the primary financial statements, are useful if they are fairly presented.

One of the requirements in paragraph 5.34 of the DP is that a performance measure should be reconciled to the most directly comparable measure specified in IFRS Standards to enable users of financial statements to see how the performance measure has been calculated. However, paragraph 5.34 then goes on to say that if the reconciliation is not possible, the notes must contain an explanation of why not. We do not agree with paragraph 5.34(c)(ii). We think that if the reconciliation cannot be done, then the performance measure should not be presented in the financial statements.

We note that the FMA (NZ Regulator) has recently published updated guidance on disclosing non-GAAP financial information outside of the financial statements.<sup>9</sup> The principles in the guidance are very similar to those requirements proposed in the DP for the fair presentation of performance measures.

We suggest the IASB considers redrafting the requirement in paragraph 5.34 (c) (i) to require disclosure of the “objective” of the performance measure i.e. how the performance measure assists users in evaluating and understanding the entity’s performance for the period.

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<sup>9</sup> <https://fma.govt.nz/assets/Guidance/versions/3406/120901-guidance-note-disclosing-non-gaap-financial-information.2.pdf>

## Section 6—Disclosure of accounting policies

### Question 10

The IASB's preliminary views are that:

- a general disclosure standard should include requirements on determining which accounting policies to disclose as described in paragraph 6.16; and
  - the following guidance on the location of accounting policy disclosures should be included either in a general disclosure standard or in non-mandatory guidance (or in a combination of both):
    - the alternatives for locating accounting policy disclosures, as described in paragraphs 6.22–6.24; and
    - the presumption that entities disclose information about significant judgements and assumptions adjacent to disclosures about related accounting policies, unless another organisation is more appropriate.
- (a) Do you agree with the IASB's preliminary view that a general disclosure standard should include requirements on determining which accounting policies to disclose as described in paragraph 6.16? Why or why not? If you do not agree, what alternative proposal(s) do you suggest, and why?
- (b) Do you agree with the IASB's preliminary view on developing guidance on the location of accounting policy disclosures? Why or why not? Do you think this guidance should be included in a general disclosure standard or non-mandatory guidance (or in a combination of both)? Why?

If you support the issuance of non-mandatory guidance in Question 10(b), please specify the form of non-mandatory guidance you suggest (listed in paragraphs 2.13(a)–(c)) and give your reasoning.

### Question 10(a)

We partly agree with the IASB's preliminary view that a general disclosure standard should include requirements on determining which accounting policies to disclose as described in paragraph 6.16.

We agree that a general disclosure standard should explain the objective of providing accounting policy disclosures, and agree with the objective set-out paragraph 6.16(a) of the DP.

We agree with paragraph 6.16(c) of the DP, that the disclosure of immaterial accounting policies should not be required (but also not prohibited) and that an entity should not allow the disclosure of immaterial accounting policies to obscure material information or to make the financial statements more difficult to understand.

We do not agree with the IASB's preliminary view in paragraph 6.16(b) of the DP, to describe the three categories of accounting policies. We believe that the introduction of the three categories would create unnecessary complexity. In our view, the disclosure of all material accounting policies should be required, making it unnecessary to distinguish between the three categories of accounting policies. We recommend that the IASB considers amendments to IAS 1 *Presentation of Financial Statements* to require the disclosure of material accounting policies, as opposed to significant accounting policies. We believe that this would remove confusion regarding the meaning of significant and would place greater emphasis on the application of materiality when making accounting policy disclosures.

In theory, we agree that the disclosure of accounting policies in Category 1 (material accounting policies where the entity has made a choice between alternatives or applied significant judgements/assumptions) should be required in the financial statements.

Regarding the disclosure of Category 2 accounting policies, we have received mixed views from New Zealand constituents as to whether disclosure of accounting policies in Category 2 should be required. Those that support only requiring disclosure of accounting policies in Category 1 observed that users are interested in understanding where/how accounting policies differ between entities, rather than “standard” IFRS requirements. Those that support disclosure of accounting policies in both Category 1 and Category 2 believe disclosure of all material accounting policies is necessary for the financial statements to be understandable as a standalone document and by users who are not familiar with the requirements of IFRS Standards.

*Question 10(b)*

We do not believe that additional guidance is needed regarding the location of accounting policies. We consider that paragraphs 113–114 of IAS 1 contain sufficient guidance regarding the ordering and grouping of the notes.

113	<b>An entity shall, as far as practicable, present notes in a systematic manner. In determining a systematic manner, the entity shall consider the effect on the understandability and comparability of its financial statements. An entity shall cross-reference each item in the statements of financial position and in the statement(s) of profit or loss and other comprehensive income, and in the statements of changes in equity and of cash flows to any related information in the notes.</b>
114	<p>Examples of systematic ordering or grouping of the notes include:</p> <ul style="list-style-type: none"> <li>(a) giving prominence to the areas of its activities that the entity considers to be most relevant to an understanding of its financial performance and financial position, such as grouping together information about particular operating activities;</li> <li>(b) grouping together information about items measured similarly such as assets measured at fair value; or</li> <li>(c) following the order of the line items in the statement(s) of profit or loss and other comprehensive income and the statement of financial position, such as: <ul style="list-style-type: none"> <li>(i) statement of compliance with IFRSs (see paragraph 16);</li> <li>(ii) significant accounting policies applied (see paragraph 117);</li> <li>(i) supporting information for items presented in the statements of financial position and in the statement(s) of profit or loss and other comprehensive income and in the statements of changes in equity and of cash flows, in the order in which each statement and each line item is presented; and</li> <li>(ii) other disclosures, including: <ul style="list-style-type: none"> <li>(1) contingent liabilities (see NZ IAS 37) and unrecognised contractual commitments, and</li> <li>(2) non-financial disclosures, eg the entity’s financial risk management objectives and policies (see NZ IFRS 7).</li> </ul> </li> </ul> </li> </ul>

We also do not agree with the IASB’s preliminary view that significant judgements and assumptions should be disclosed adjacent to the related accounting policies. We have heard that some users of financial statements prefer information about significant judgements and assumptions to be located in a separate section at the front of the notes. Therefore, we do not think that the IASB should



restrict an entity from providing disclosures of significant judgements and assumptions in a format that may better reflect the needs of the users of its financial statements.

**Section 7—Centralised disclosure objectives**

**Question 11**

The IASB's preliminary view is that it should develop a central set of disclosure objectives (centralised disclosure objectives) that consider the objective of financial statements and the role of the notes.

Centralised disclosure objectives could be used by the IASB as a basis for developing disclosure objectives and requirements in Standards that are more unified and better linked to the overall objective of financial statements.

Do you agree that the IASB should develop centralised disclosure objectives? Why or why not? If you do not agree, what alternative do you suggest, and why?

We agree that the IASB should develop centralised disclosure objectives (for the reasons given by the IASB in paragraph 7.10 of the DP).

**Question 12**

The IASB has identified, but not formed any preliminary views about, the following two methods that could be used for developing centralised disclosure objectives and therefore used as the basis for developing and organising disclosure objectives and requirements in Standards:

- focusing on the different types of information disclosed about an entity's assets, liabilities, equity, income and expenses (Method A); or
- focusing on information about an entity's activities to better reflect how users commonly assess the prospects for future net cash inflows to an entity and management's stewardship of that entity's resources (Method B).

(a) Which of these methods do you support, and why?

(b) Can you think of any other methods that could be used? If you support a different method, please describe your method and explain why you think it might be preferable to the methods described in this section.

Methods A and B are in the early stages of development and have not been discussed in detail by the IASB. We will consider the feedback received on this Discussion Paper about how centralised disclosure objectives might best be developed before developing them further.

*Question 12(a)*

We do not consider that Method B has been sufficiently developed to allow us to make an informed decision regarding which method we support.

*Question 12 (b)*

We have not identified any other methods that could be used. We note that Method B would have to be a hybrid of Method A and Method B as information about the basis of preparation of the financial statements is identified as a "type of information" under Method A and centralised disclosure objectives would need to be developed for this type of information even if Method B "entity's activities" is used to develop centralised disclosure objectives.

**Question 13**

Do you think that the IASB should consider locating all disclosure objectives and requirements in IFRS Standards within a single Standard, or set of Standards, for disclosures? Why or why not?

We support locating all disclosure objectives and requirements within a single IFRS Standard. We believe locating all disclosures in a single IFRS Standard would encourage more discipline in how the IASB sets disclosure requirements, because all disclosure requirements would be considered in relation to each other, instead of the focus being on an individual standard. We also believe that this approach would be more user-friendly, reduce duplications and would better highlight the relationships between disclosure requirements.

This approach will also help preparers to take a more holistic approach to disclosures rather than a piecemeal approach and therefore hopefully will have the added benefit of changing the behaviour of stakeholders.

We note that if the IASB adopted Method B for developing centralised disclosure objectives it would likely have to locate disclosure objectives and requirements within a single Standard.

Thinking to the future, the IASB will need to consider how IFRS Standards will be made available and whether they will be consumed in a digital interactive format. Such a format might allow for disclosure requirements to be filtered from other recognition and measurement requirements. Should IFRS Standards be made available in such a format the location of where disclosure objectives and requirements are located will become less relevant.

**Section 8—New Zealand Accounting Standards Board staff’s approach to drafting disclosure requirements in IFRS Standards**

**Question 14**

This section describes an approach that has been suggested by the NZASB staff for drafting disclosure objectives and requirements in IFRS Standards.

- (a) Do you have any comments on the NZASB staff’s approach to drafting disclosure objectives and requirements in IFRS Standards described in this section (the main features of the approach are summarised in paragraph 8.2 of this section)?
- (b) Do you think that the development of such an approach would encourage more effective disclosures?
- (c) Do you think the IASB should consider the NZASB staff’s approach (or aspects of the approach) in its Standards-level Review of Disclosures project? Why or why not?

Note that the IASB is seeking feedback on the NZASB staff’s overall approach, rather than feedback on the detailed drafting of the paragraphs on the use of judgement in the NZASB staff’s example 1 or the detailed drafting of the specific disclosure requirements and objectives included in the NZASB staff’s examples 2 and 3. In addition, the IASB is not seeking feedback on where specific disclosure objectives and requirements should be located in IFRS Standards (except as specifically requested in Question 13).

*Question 14(a)*

Overall, we support the development of a unified and consistent approach to drafting disclosure requirements in IFRS Standards, which emphasises the application of judgement.

Disclosure objectives

We support the development of disclosure objectives and subobjectives when drafting disclosure requirements in IFRS Standards. The inclusion of objectives and subobjectives which explain why users need particular types of information will:

- (a) help preparers better understand the objective of a disclosure requirement and assist in applying judgement when deciding what information to disclose; and
- (b) impose a greater level of discipline on the IASB when drafting disclosure requirements.

We support having an overall disclosure objective for each standard that is based on the objective of financial statements. In our view, this emphasises the objective of financial reporting and provides a clear link between: (a) the objective of financial reporting; and (b) the subobjectives and the particular set of disclosure requirements in the standard (as the particular set of disclosure requirements should link with the applicable subobjective, and each subobjective should link with the overall objective). This should promote consistency between that overall objective, the subobjectives, the individual disclosure requirements and the objective of financial reporting.

However, it is important that the subobjectives are not drafted in generic terms. By generic terms we mean they should not just be a copy of the objective of financial statements. The subobjectives need to clearly explain why users need particular types of information. NZASB staff have acknowledged the challenges in drafting the subobjectives in the staff examples provided in the DP.

We have received feedback from New Zealand constituents that in some cases the disclosure subobjectives could be improved. Development of the subobjectives will impose a discipline on the standard setter because if the standard setter is not able to articulate why users need particular types of information then you could argue that the disclosure may not be needed.

#### Tiers of disclosure requirements

We support having two tiers of disclosure requirements. Firstly, the two-tier approach provides a balance between ensuring a level of comparability between entities (through tier 1 disclosure requirements) and providing the flexibility for entities to apply judgement to determine relevant information to disclose (through tier 2 disclosure requirements). Secondly, we believe that the two-tier approach, compared with the current drafting of disclosure requirements, better encourages preparers to exercise judgements about materiality when making disclosures.

We note the following concerns raised by New Zealand constituents with the two-tier approach.

- (a) It may be difficult for the IASB to distinguish between summary and additional information, therefore making the approach difficult to operationalise.
- (b) Some constituents felt that having two tiers of disclosure requirements was unnecessary. They considered that the proper application of materiality to one set of disclosure requirements could result in a similar outcome.
- (c) The two-tier approach requires more time and effort to apply than a more prescriptive disclosure approach.
- (d) The two-tier approach allows entities too much flexibility and will lead to a loss in comparability between entities.

While we acknowledge these concerns, we are still supportive of the two-tier approach. If the IASB and some constituents are concerned about the extent of judgement preparers would be permitted to exercise with the second tier, an alternative would be to re-frame the two-tier approach with the “CORE & MORE” approach discussed in our response to question 2.

Under a CORE & MORE approach, summary information would be presented in the CORE report and additional information that an entity determines is less relevant to users would be included in the MORE report(s).

#### Emphasis on need to exercise judgement

We strongly support the inclusion of paragraphs to emphasise the use of judgement. We consider behavioural issues in applying judgement to be a significant contributor to the disclosure problem. We believe that emphasising the use of judgement through the inclusion of such paragraphs will help to encourage preparers to apply judgement.

Our preference would be for these paragraphs to be included in each standard that contains disclosure requirements, rather than just in a general disclosure standard. While this will result in repetition we believe that the benefit of greater visibility will exceed the cost of repetition.

### Less prescriptive language

We support the use of less prescriptive language when drafting disclosure requirements. We have received feedback from New Zealand constituents that the use of “shall” is interpreted by some stakeholders as implying that materiality does not apply.

We believe that the use of less prescriptive language would help dispel this misunderstanding and lead to less irrelevant disclosures being made in the financial statements.

### *Question 14(b)*

As noted in our response in Section 1, we consider that behavioural issues in applying judgement may play a greater role in contributing to the disclosure problem, rather than existing requirements.

However, we think that the development of the NZASB staff’s approach would encourage more effective disclosures as a result of:

- (a) imposing a greater level of discipline on the IASB to ensure each disclosure requirement is linked to a disclosure subobjective. The need to provide clear disclosure subobjectives, should focus the IASB’s attention on:
  - (i) the purpose of each disclosure requirement; and
  - (ii) considering whether disclosure requirements contribute to meeting that purpose; and
- (b) encouraging preparers to apply judgement through the use of less prescriptive wording and the inclusion of paragraphs emphasising the use of judgement.

We also believe that this approach will help drive a positive change in behaviour from wider stakeholders, which will give preparers greater confidence to exercise judgement.

### *Question 14(c)*

We think that the IASB should consider the NZASB staff’s approach in its Standards-level Review of Disclosures project, for the reasons identified in our response to questions 14(a) and (b) above.

### **Question 15**

Some stakeholders say that the way that disclosures are drafted in IFRS Standards might contribute to the “disclosure problem”, as described in Section 1. Some cite in particular the absence of clear disclosure objectives and the presence of long lists of prescriptively written disclosure requirements in Standards (see paragraph 8.4).

Nevertheless, other stakeholders observe that specific disclosure requirements might be simpler to use than applying judgement when determining how to meet disclosure objectives.

Do you think the way the IASB currently drafts IFRS Standards contributes to the disclosure problem? Please give your reasoning. If you think the current drafting contributes to the disclosure problem, please provide examples of where drafting in Standards could be improved and why.

We think that the way the IASB currently drafts disclosure requirements in IFRS Standards has contributed to the disclosure problem. As noted by the IASB in the DP and discussed in our response to question 14, we consider the lack of clear disclosure objectives and the use of prescriptive language as contributing factors to the disclosure problem.

*Examples of where drafting in Standards could be improved*

Examples of prescriptive language can be found throughout IFRS Standards, and include the use of “An entity shall disclose”, “an entity shall disclose, as a minimum”, “the following shall be disclosed” or other similar prescriptive language.

*IFRS 12 Disclosure of Interests in Other Entities*

<b>21</b>	<p><b>An entity shall disclose:</b></p> <ul style="list-style-type: none"> <li>(a) for each joint arrangement and associate that is material to the reporting entity: <ul style="list-style-type: none"> <li>(i) .....</li> </ul> </li> </ul>
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We have heard that the inclusion of the word “material” along with the prescriptive wording in the drafting of paragraph 21 of IFRS 12 causes confusion for preparers. Some preparers have interpreted paragraph 21 of IFRS 12 to require an entity make *all* the disclosures listed, even if the information resulting from an individual disclosure is not material, as long as the joint arrangement or associate is itself material to the reporting entity.

As noted in our response to question 4, we believe that greater emphasis on materiality is needed when drafting disclosure requirements. However, care needs to be taken when doing so. In particular, to avoid similar problems as currently arises with the drafting in IFRS 12, we do not believe that referencing materiality in specific disclosure requirements is helpful. Materiality is a pervasive concept and it adds confusion to preparers if it is scattered throughout disclosure requirements. Hence, we recommend providing greater emphasis on materiality in a manner that reinforces materiality as a pervasive concept, e.g. by including a general paragraph in each standard reminding entities to apply materiality or with appropriate cross-references to the relevant parts of IAS 1 (or its replacement).



NZ ACCOUNTING  
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## Memorandum

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**Date:** 1 September 2017

**To:** NZASB Members

**From:** Anthony Heffernan

**Subject:** Board preparation for discussion with Big 4 Chief Executives/Managing Partners

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### Introduction<sup>1</sup>

1. We have invited the Chief Executives/Managing Partners from the “big 4” accountancy firms to our September NZASB meeting for a 60-minute discussion with the Board on the *Future of Financial Reporting*.
2. In preparation for this agenda item, Board members are asked to CONSIDER questions they may want to ask the big 4 Chief Executives/Managing Partners during this non-public session of the NZASB meeting.
3. The big 4 Chief Executives/Managing Partners will provide valuable insights into the future of financial reporting, including the future challenges and opportunities.
4. The key objective of the session is to hear the views of the big 4 Chief Executives/Managing Partners on the expected challenges and opportunities arising from the future of financial reporting. We are expecting the discussion with the Board will flow naturally. Therefore, this Board paper has been prepared for Board preparation purposes only and should not be considered a formal “run sheet” of questions.

### Purpose of agenda item

5. Our NZASB Strategic Action Plan 2017–2022 includes an action to meet with our major constituent groups as part of the Board’s regular meetings.<sup>2</sup>
6. The purpose of this strategy is to increase the level of constituent engagement to ensure that our standards continue to be developed with constituents in a collaborative manner. Meeting with major constituent groups at the Board level provides the Board with an understanding of emerging trends in future financial reporting developments and any current implementation issues in practice.
7. To action this strategy, we have invited the Chief Executives/Managing Partners from the big 4 accountancy firms to our September NZASB meeting. Staff are meeting with

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<sup>1</sup> This memo refers to the work of the International Accounting Standards Board (IASB) and uses registered trademarks of the IFRS Foundation (for example, IFRS® Standards, IFRIC® Interpretations and IASB® papers).

<sup>2</sup> Action 4A.2(a) of the NZASB Strategic Action Plan 2017–2022.

representatives of the “mid-tier” accounting firms on a regular basis and we will consider in the future inviting the Chief Executives/Managing Partners of these firms to an NZASB meeting.

8. The big 4 accountancy firms are an important constituent group as they represent both preparers and users of general purpose financial statements. These firms provide professional accountancy services to the majority of NZX listed companies (and other for-profit Tier 1 entities), as well as many other private companies and public benefit entities in New Zealand.
9. We are expecting<sup>3</sup> the following representatives from from the big 4 accountancy firms to attend the NZASB meeting as guests for this agenda item.
  - (a) EY – Simon O’Connor - New Zealand Managing Partner
  - (b) Deloitte – Peter Gulliver - National Leader - Assurance & Advisory
  - (c) KPMG – Graeme Edwards - National Managing Partner Audit
  - (d) PwC – Jonathan Freeman - New Zealand Assurance Managing Partner

#### **Focus of Chief Executive/Managing Partner discussion**

10. The invitation sent to the big 4 Chief Executives/Managing Partners to attend the NZASB September meeting was titled, *The Future of Financial Reporting from the Perspective of a Big 4 Chief Executive/Managing Partner*, and attendees have been invited to share their views on:
  - (a) supporting the development of accounting standards that meet current and future user needs, enhance investor confidence and enable New Zealand companies to compete internationally;
  - (b) enhancing the communication effectiveness of financial statements;
  - (c) future challenges and opportunities to improve the relevance and usefulness of information reported in financial statements (e.g. impact of digital disruption, demand for real time information, use of digital technologies allowing the user to tailor and design the information they receive, and the rise of integrated reporting); and
  - (d) if time permits, current accounting issues impacting for-profit reporting in New Zealand.
11. The invitation noted that we wish the discussion to focus on the perspective of the Chief Executive/Managing Partner, rather than the perspective of a Technical Partner/Director.
12. The focus of the discussion is on the future of financial reporting from a for-profit Tier 1 perspective.

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<sup>3</sup> Subject to any last-minute changes.



## Questions from the Board

13. In preparation for the 60-minute discussion with the big 4 Chief Executives/Managing Partners, we suggest Board members consider questions they may want to raise during this non-public session of the agenda.
14. The following are some ideas of possible questions. They have been drafted at a high-level to encourage a broad response, rather than questions that may lead to a technical discussion.
15. The possible questions are based around the broad topics provided in the meeting invitation. The discussion on the day could easily go in a different direction, the focus will be on hearing the attendees' views on the impact of expected future financial reporting developments.

## Supporting the development of accounting standards

16. The accounting standards applied by Tier 1 for-profit entities comprise the requirements of IFRS Standards as issued by the IASB, plus some additional NZ-specific disclosures (referred to as NZ IFRS). In the for-profit sector, the NZASB is therefore largely considered a "standard taker" when developing and issuing standards.
17. Under this topic it would be useful for the Board to understand how it can enhance the engagement and support it receives from the big 4 accountancy firms in the NZASB's standard-setting process.

- Q1. What actions would you recommend the NZASB take to promote the awareness of IASB and domestic due process documents issued and to encourage input<sup>4</sup> from accountancy firms in New Zealand – especially for areas of particular interest to New Zealand constituents?
- Q2. Are there any other suggestions for recommended NZASB actions to support the development of accounting standards that meet current and future user needs and enhance investor confidence [in addition to current XRB research projects on user-needs)?

## Enhancing the communication effectiveness of financial statements

18. The IASB has a current strategic focus on enhancing the communication effectiveness of financial statements<sup>5</sup>, by developing reporting requirements and principles that support the presentation of financial information in financial statements that is relevant and useful to investors when making decisions.
19. On their own initiative, we note a number of New Zealand for-profit companies have already embarked on streamlining projects and have achieved substantial reductions in the length and complexity of their financial statements. This has been achieved by preparers focusing

<sup>4</sup> Some of the firms aren't permitted to make local submissions on IFRS proposals, as the firm has a single global view. Hence, the question has been phrased more broadly to refer to input, rather than submissions.

<sup>5</sup> Includes the following IASB Projects – *Principles of Disclosure*, *Primary Financial Statements* and *Definition of Material*, and encompasses the overall "disclosure initiative".

on the disclosures of greater relevance and importance to users, and the removal of unnecessary information in financial statements.

Q3. The IASB has previously noted, a common complaint from companies applying IFRS is that they are required to disclose irrelevant information, which unnecessarily adds to the preparation costs and page count of financial information and ultimately does not lead to the presentation of useful information.

In your view, as an outcome of the recent focus of removing unnecessary information and streamlining disclosures in the financial statements, have you noted an improvement in the communication effectiveness of the general purpose financial statements of for-profit companies in New Zealand (i.e. an improved focus on areas of most relevance and importance to users)?

Q4. Has the focus on decluttering the information disclosed in general purpose financial statements resulted in the loss of some financial information that was previously disclosed that was considered useful by some users (for example, financial analysts)?

Q5. To further improve the communication effectiveness of financial statements, what would you suggest the next area of focus by the IASB/NZASB should be?

Question 5 is open ended, you may want to consider asking a more specific question on whether they think there's a need for improvements to the presentation of performance measures in the income statement, especially given the growth in alternative performance measures (APMs). Should standard-setters be seeking to promote the consistent use of APMs (such as gross profit, operating profit and EBITDA) or should preparers have the flexibility to use sub-totals in the income statement that they consider best meet user needs?

Future challenges and opportunities to improve the relevance and usefulness of information reported in financial statements

20. Current and future technological developments (and the increasing use of artificial intelligence) are expected to soon provide automated integrated solutions that will change users' expectations of the timing and methods in which they receive financial information, which will be much broader than the conventional printed general purpose financial statements.

Q6. In your view, what will general purpose financial information for for-profit companies look like in the next 5–10 years (for example, demand for real time information, use of digital technologies allowing the user to tailor and design the information they receive)?

Q7. In your view, do you expect there will still be a need for the preparation of traditional year/period-end general purpose financial statements in the future?

21. The NZASB currently has a strategic focus on promoting the awareness, understanding and development of extended external reporting (EER)<sup>6</sup> among New Zealand constituents.
22. The NZASB recognises that EER is a subject of growing prominence and importance, although much of it is currently prepared on a voluntary basis both in New Zealand and overseas. The XRB has noted an increased expectation from users (including regulators, investors and analysts) that companies should report on a broader range of factors beyond purely financial results. Moreover, internationally it is considered there is an appetite for some standardisation and several global reporting frameworks for EER type information have been developed in response to this.

- Q9. In your view, what is the current expectation of users both in New Zealand and internationally around the reporting of EER type information, and are there any emerging trends?
- Q10. In your view, what role should standard-setters (such as the IASB and NZASB) be taking in promoting the consistent reporting of EER type information? Should the IASB/NZASB be developing principles and requirements for the presentation of financial information provided in the annual report, but outside the financial statements?

Current accounting issues impacting for-profit reporting in New Zealand

23. This final topic for discussion is a general catch-all of any other current issues or questions, which can be discussed if time permits.

- Q11. Are there any other current IFRS application issues or areas where additional guidance should be developed by the IASB to promote the consistent application of NZ IFRS in New Zealand?

**Recommendation**

24. We recommend that the Board, in preparation for the discussion with the big 4 Chief Executives/Managing Partners, CONSIDER questions they may want to raise during this agenda item.

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<sup>6</sup> Described by the IASB as “wider corporate reporting”, which is a broad term used to refer to any reporting by entities that falls outside the primary financial statements and the notes, and includes integrated reporting, sustainability reporting, management discussion and analysis (MD&A) etc.



NZ ACCOUNTING  
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## Memorandum

**Date:** 1 September 2017  
**To:** NZASB Members  
**From:** Joanne Scott and Lisa Kelsey  
**Subject:** **Service Performance Reporting: Analysis of submissions**

### Action required<sup>1</sup>

1. In this item the Board is asked to:
  - (a) RECEIVE a verbal update on a meeting of NZASB and NZAuASB service performance subcommittee members, held on 5 September. The verbal update is agenda item 6.1. See also agenda item 2.9;
  - (b) CONSIDER submissions received on the limited scope review draft of PBE FRS XX *Service Performance Reporting* (the draft standard). This memo discusses the issues arising from the submissions. An analysis of the submissions is set out in agenda item 6.3. Copies of submissions are available in agenda item 6.4 in the supporting papers; and
  - (c) AGREE changes to the draft standard in response to comments received. The draft standard, showing marked-up changes, is agenda item 6.5.
2. We are hoping to get sufficient direction at this meeting to finalise the drafting changes and seek approval to issue the standard at the NZASB meeting on 1 November.

### Background

3. In February 2016 the NZASB issued an exposure draft of a new service performance reporting standard for Tier 1 and 2 public benefit entities (PBEs). Table 1 outlines the steps since then.

**Table 1 Project history**

Date	Details
Feb 2016	ED NZASB 2016-6 <i>Service Performance Reporting</i> (2016 ED) issued.
Feb–July 2016	Outreach on the 2016 ED.
29 July 2016	Closing date for submissions on the 2016 ED. 18 submissions received.
26 Aug 2016	NZAuASB subcommittee provides feedback to the NZASB subcommittee on the 2016 ED.

<sup>1</sup> This memo refers to the work of the International Accounting Standards Board (IASB) and uses registered trademarks of the IFRS Foundation (for example, IFRS® Standards, IFRIC® Interpretations and IASB® papers).

Date	Details
15 Sept 2016	The Board considered submissions on the ED and feedback from the NZAuASB subcommittee. The Board provided feedback on how to move forward with this project. The Board agreed to remove some detailed requirements and develop a more principles-based standard.
3 Nov 2016	The Board provided feedback on the revised draft, focussing on the sections dealing with information to be reported and disclosure of judgements.
15 Dec 2016	The Board provided feedback on the sections dealing with information to be reported and disclosure of judgements.
24 Feb 2017	NZASB subcommittee provided feedback on the sections dealing with information to be reported and disclosure of judgements.
22 Mar 2017	The Board provided feedback on the sections dealing with information to be reported, disclosure of judgements, presentation and comparatives. The Board agreed to consider the whole standard and due process steps in May 2017.  Staff were directed to prepare fatal flaw review papers for May and to organise a meeting of the NZASB and NZAuASB subcommittees.
27 April 2017	NZASB and NZAuASB subcommittees met on 27 April 2017.  The agenda papers included draft agenda papers for the NZASB May meeting and a report back on how previous NZAuASB comments had been addressed. NZAuASB members were generally supportive of the draft standard but noted that the high-level approach had implications for the auditing standard.
4 May 2017	The Board considered the remaining issues raised in submissions on the 2016 ED.  The Board considered due process. It considered whether to re-expose its revised proposals or undertake some other form of consultation on the changes made since the 2016 ED. The Board agreed to undertake a limited scope consultation.
24 May 2017	Limited scope review draft issued.  Feedback statement made available on website (see agenda item 6.7).
End May 2017	Letter sent to respondents to the 2016 ED and ten other interested parties (see agenda item 6.6).
28 July 2017	Closing date for submissions on the limited scope review draft.  12 submissions received.
5 Sept 2017	NZASB and NZAuASB joint subcommittee meeting. Suggestions for improving the draft accounting standard (to be considered at the joint subcommittee meeting) are also shown in agenda item 6.5.  We will provide a verbal update on this meeting.

### Structure of this memo

4. Our objective at this meeting is to get sufficient direction on how we have responded to comments from constituents and the joint subcommittee meeting to finalise the accounting standard in November. We therefore need to consider:
  - (a) the joint subcommittees' response to the suggestions for improving the draft accounting standard; and
  - (b) the submissions received on the limited scope review draft.
5. The remainder of this memo is set out as follows.
  - (a) Submissions received;
  - (b) Issues 1–9;
  - (c) Recommendations; and
  - (d) Next steps.

### Submissions received

6. The limited scope review draft ED contained the following question for constituents. This question signalled the limited scope of the consultation.

Taking into account the proposals in the 2016 ED, the comments received and the changes made in response to those comments, do you have any comments on the workability of the revised proposals or whether they would have any unintended consequences?

7. The list of submissions is set out in Table 2. Most of the responses on the limited scope review draft were supportive, but respondents also suggested improvements and raised matters for consideration by the Board. Because of the nature of the question posed, and the fact that most of the submitters had previously submitted on the 2016 ED, some of the responses are fairly brief.

**Table 2: Submissions received**

R#	Respondent	Submitted on the 2016 ED	Agenda item
R1	Trade Aid Importers Ltd	–	6.4.1
R2	Carolyn Cordery	✓	6.4.2
R3	RSM	✓	6.4.3
R4	The Treasury	✓	6.4.4
R5	CA ANZ	✓	6.4.5
R6	OAG and Audit NZ	✓	6.4.6
R7	Dr Cherrie Yang	✓	6.4.7
R8	Commerce Commission and the Electricity Authority	✓	6.4.8

R#	Respondent	Submitted on the 2016 ED	Agenda item
R9	IOD	✓	6.4.9
R10	EY	✓	6.4.10
R11	Auckland City Council	✓	6.4.11
R12	Confidential	–	2.3.4

8. Agenda item 6.3 contains respondents' comments and the staff response. Copies of the individual submissions are including in the supporting papers at agenda item 6.4. The issues that we have identified for consideration by the Board are:
- (a) Issue 1: Subcommittee issues (QCs and disclosures);
  - (b) Issue 2: Scope;
  - (c) Issue 3: Structure/Definitions;
  - (d) Issue 4: Cost of goods and services;
  - (e) Issue 5: Effective date;
  - (f) Issue 6: Amendments to PBE FRS 42;
  - (g) Issue 7: Comments on guidance;
  - (h) Issue 8: Post-implementation review; and
  - (i) Issue 9: Difference between Tiers.
9. At the end of each issue we seek direction from the Board on how we should proceed.

**Issue 1: Subcommittee issues (QCs and disclosures)**

10. As noted above, some suggestions for improving the accounting standard will be discussed by NZASB and NZAuASB subcommittee members on 5 September (see also agenda item 2.9). We will provide a verbal update on that meeting to the NZASB.
11. We have identified possible improvements to the sections of the draft accounting standard dealing with qualitative characteristics and disclosure of judgements.

*Qualitative characteristics*

12. Auditing standards and accounting standards use different terms for the qualitative characteristics. We have considered whether the key aspects of the qualitative characteristics (in both sets of standards) are clear enough in the draft accounting standard. We have suggested expanding the descriptions of faithful representation and verifiability. The proposed changes to paragraph 9(b) and (f) of the draft accounting standard are set out in agenda item 6.5.

*Disclosure of judgements*

13. Respondents were very supportive of the new section about disclosure of judgements. Some have queried whether the disclosure requirements go far enough. Some (paraphrased) comments from respondents are as follows.
  - (a) R3 noted some auditing challenges associated with the high-level principle-based approach in the draft accounting standard. R3 sees the requirement for a preparer to disclose critical judgements as vitally important. However, R3 has a concern about how the term “critical” will be interpreted by preparers. R3’s concern is that some may not disclose otherwise important or significant information as they don’t assess this as critical.
  - (b) R5 expressed the view that the requirement to disclose critical judgements in paragraph 44 is essential.
  - (c) R6 noted that some performance measures may involve complex methodologies and key judgements. R6 requested that the NZASB consider some level of disclosure about judgements made in measuring performance (plus perhaps methodologies and assumptions).
  - (d) R7 supported the proposals in the limited scope review draft.
  - (e) R9 noted that the new disclosure requirements are a consequence of the less prescriptive approach to the information to be reported and agreed that it is a necessary counterbalance for a more flexible framework for reporting information. R9 also commented that information must be meaningful for the entity and cautioned against requiring too much information.
  - (f) R10 was supportive of the high-level approach in the draft standard and felt that some of the risks associated with this approach (important information being omitted) would be mitigated by the disclosure requirements. R10 also noted that the higher-level approach could reduce comparability across entities and considered that the disclosure requirements would help mitigate this risk.
14. The comments from R3 and R6, together with internal discussions about how this standard will work with the forthcoming auditing standard, have led us to suggest some improvements to the Disclosure of Judgements section (paragraphs 44–46) with the aim of making the requirements more robust. The proposed changes are shown as marked-up text in agenda item 6.5. A possible variation on paragraph 44 wording was also included in agenda item 2.9.

Q1. Having regard to respondents’ comments and feedback from the joint subcommittee meeting, does the NZASB support the proposed changes to the qualitative characteristics and the disclosure requirements (in agenda item 6.5)?



## Issue 2: Scope

15. R5 commented on the proposed scope and recommended removing the reference to GAAP. R5 said:

Paragraph 3(b) refers to “*Tier 1 and Tier 2 public sector public benefit entities required by legislation to provide information in respect of service performance in accordance with generally accepted accounting practice (GAAP)*”. The reference to GAAP will scope out some entities where legislation does not explicitly reference GAAP such as council-controlled organisations under section 68 of the Local Government Act 2002 and school boards under section 87 of the Education Act 1989. On this basis we recommend removing the reference to GAAP so that all Tier 1 and Tier 2 public sector public benefit entities required by legislation to provide information in respect of service performance must do so in accordance with the standard.

16. We propose no change in response to this comment. As explained below, the reference to GAAP was a deliberate addition following consideration of respondents’ comments on the 2016 ED.
17. The scope of the draft standard has been debated extensively over the life of this project and the key factors considered by the Board (including the differing legislative reporting requirements for different types of entities) are outlined in the Basis for Conclusions. To recap on the development of the scope requirements, we have noted what the 2016 ED said and the changes made following consideration of respondents’ comments on the 2016 ED.

### Extract from 2016 ED

21. This [draft] Standard applies to all Tier 1 and Tier 2 not-for-profit public benefit entities. It also applies to Tier 1 and Tier 2 public sector public benefit entities which are required by legislation to provide a statement of service performance (by whatever name called).

### Extract from the limited scope review draft

#### 3. This Standard applies to:

- (a) **All Tier 1 and Tier 2 not-for-profit public benefit entities; and**
- (b) **Tier 1 and Tier 2 public sector public benefit entities required by legislation to provide information in respect of service performance in accordance with generally accepted accounting practice (GAAP). If an entity is required by legislation to report service performance information on only some of its activities, this Standard applies only to those activities.**

18. Following consideration of comments on the 2016 ED, the Board agreed the following changes to the scope requirements. The reasons for those changes are shown in brackets.
  - (a) Limit the public sector scope to legislative reporting requirements that refer to GAAP. (Not all legislative requirements refer to GAAP.)
  - (b) Limit the public sector scope to the activities of an entity that are subject to legislative reporting requirements. (Not all activities of an entity may be subject to legislative performance reporting requirements.)
  - (c) In the public sector scope requirement, refer to “information in respect of service performance” rather than “a statement of service performance” (by whatever name

called).” (References to statements of service performance have been dropped from some legislation.)

19. The first two changes were to better align the scope requirements with the existing legislative requirements. These changes were seen as being consistent with, and clarifications of, the NZASB’s intentions when it issued the 2016 ED. We therefore propose no further changes to the scope of the standard.

Q2. Does the Board agree not to change the scope requirements?

### Issue 3: Structure/Definitions

20. R2 suggested adding a definitions section and defining the terms (i) service performance information and (ii) appropriate and meaningful. R2 suggested that paragraphs 2, 22 and BC21 (see below) could be drawn upon to develop definitions.

2. Service performance information is information about what the entity has done during the reporting period in working towards its broader aims and objectives, together with supporting contextual information.

22. In selecting the performance measures and/or descriptions to be reported an entity shall consider the qualitative characteristics and the constraints on information in general purpose financial reports. Judgement is needed to determine the most appropriate and meaningful performance measures and/or descriptions to be reported. The most appropriate and meaningful performance measures and/or descriptions are those that measure aspects of performance that are of particular value or importance for accountability or decision-making purposes.

- BC1. In response to feedback received the NZASB:

- (a) clarified that the term appropriate and meaningful should be considered from the user’s point of view;
    - (b) included a discussion, from the PBE Conceptual Framework, on the trade-off needed between the qualitative characteristics; and
    - (c) emphasised the role of neutrality in faithful representation.

21. Although we acknowledge that most standards have a section dealing with definitions, we are reluctant to create defined terms in this standard. The 2016 ED included defined terms. This section was dropped following feedback that some terms are used in differing ways by different types of entities, the language used in the ED was not consistent with some outcome frameworks and there were terminology differences between the ED and some legislation.

22. A definition is the exact meaning of something. We do not think that the terms *service performance information* or *appropriate and meaningful* lend themselves to exact meanings.

Q3. Does the Board agree not to include a definitions section?

#### Issue 4: Cost of goods and services

23. R6 commented on output cost disclosure. The comment is shown below.

It is important that performance information is integrated with financial information as set out in paragraph 28 of the review draft. We do not think there will be many situations where it is not practicable for entities to disclose output costs. We think that the bar for non-disclosure of output cost information should be set at a high level. Therefore, we consider that the wording of the review draft should be strengthened to require cost disclosure related to services or activities, unless it is impracticable to do so.

24. The draft standard notes the importance of cost information, but does not mandate the reporting of cost information. Paragraph 28 from the draft standard is as follows:

28. Reporting on the cost of goods and services provides an important link between the financial statements and service performance information. However, it may not always be practicable, or the most appropriate way of reporting on goods and services. The reporting on the cost of goods and services will depend on an entity's accounting policies and its cost allocation policies. If an entity reports on the cost of goods and services it shall provide a reconciliation between the expenses in the financial statements and the total goods and services costs reported in the service performance information. Where unrecognised goods or services in-kind are a significant component of producing goods and services, any cost information provided shall also acknowledge the use of these resources. PBE IPSAS 23 *Revenue from Non-Exchange Transactions* establishes requirements for the recognition of donated goods and services.

25. The issue of whether or not cost information should be required has been discussed a number of times. Some background follows.
26. Initial drafts of the exposure draft in 2015 proposed to require cost of outputs. In June 2015 the Board considered whether cost information should be required for all outputs. The Board decided that cost of outputs is not always possible or appropriate. The Board discussed the sometimes-arbitrary nature of cost allocation and how, in some cases, the cost to the entity of providing this information could outweigh the relevance or usefulness to the user. The Board noted that it did not want to inadvertently encourage entities to only report on those outputs where a cost could be determined, and not report on a more appropriate output (this was regarded as a risk). The Board decided it should not mandate the reporting of the cost of outputs but that the standard should highlight the importance of the link between the financial statements and the service performance information. The Board also decided that where cost information is provided an entity shall provide a reconciliation between the expenses in the financial statements and the total of the output costs reported in the service performance information.
27. We propose that no changes are made to paragraph 28 of the draft standard.

<p>Q4. Does the Board agree not to change the requirements for disclosure of cost information?</p>
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## Issue 5: Effective date

28. The 2016 ED proposed a two-year period before the standard became effective. Although the majority of respondents to the 2016 ED supported the proposed two-year implementation period, some considered that two years was too short and stressed the time required to identify new measures, trial new measures and develop reliable data collection systems. They based their comments about the need for sufficient time on their experience in developing and reporting on new measures. Some respondents felt that 3 years would be better or that there should be no requirement for comparatives in the first year.
29. In the limited scope review draft the Board agreed to allow a three-year implementation period (1 January 2021) with early adoption permitted. The reasons were explained in the Basis for Conclusions.  
  
BC35. The ED proposed a two-year implementation period. Although the majority of respondents supported a two year implementation period, others requested that the NZASB consider a longer period. Those who favoured a longer period were of the view that those responsible for governance in not-for-profit entities would need time to understand the requirements and to embed service performance reporting into their planning and management processes. They also noted the time needed to develop systems to record service performance measures and the need to implement and test systems.  
  
BC36. The NZASB agreed that the Standard should have a three-year implementation period, with early adoption permitted.
30. Some respondents have commented on the proposed effective date. Some agree with the proposed effective date in the limited scope review draft, and some would prefer an earlier date. The breakdown of respondents and their paraphrased comments follow.
31. Views of respondents supporting the effective date of 1 January 2021 (R7, R9, R10):
  - R7: Agree.
  - R9: A two-year implementation period is insufficient to enable effective transition. Longer period will better support awareness raising and capability building. Better for boards and others charged with responsibility for governance (more time for understanding, better able to fulfil their responsibilities).
  - R10: Enhances the workability of the proposed standard. Gives sufficient time [for entities] to update their systems and processes and ensure that the new standard is properly implemented.
32. Views of respondents supporting an earlier effective date (R2, R3):
  - R2: This will raise the quality of reporting much more quickly and increase its comparability.
  - R3: Lost opportunity. R3 queried whether the date had been extended to align with the possible effective date of an auditing standard but did not consider that it was essential for the accounting and auditing standards to have the same effective date.

33. We consider that the Board should keep the effective date (1 January 2021) proposed in the limited scope review draft for the following reasons.
- (a) As explained in the Basis for Conclusions, the effective date of 1 January 2021 was in response to comments from some constituents on the 2016 ED that the original proposal was too tight.
  - (b) A key factor affecting the ability of an entity to report in accordance with the new standard is whether it needs to identify and trial new measures and how long this will take. Some entities, particularly NFPs, will need to identify and trial new measures.
  - (c) Some respondents explicitly commented that the longer period is necessary and desirable.
  - (d) The lost opportunity of a later effective date needs to be balanced against the risk that it would not be feasible for others.

Q5. Does the Board agree that the standard should have an effective date of 1 January 2021, with early adoption permitted?

#### Issue 6: Amendments to PBE FRS 42

34. One respondent (R6) disagreed with the proposed amendments to PBE FRS 42 and felt that the amendments might have an unintended consequence. R6 recommended that the NZASB not amend PBE FRS 42 as part of this project. Instead, R6 proposed that the NZASB carry out further work to determine how best to cater for prospective service performance information. R6's comments are shown below.

##### **R6's comments**

Prospective service performance information is different to prospective financial statement information.

Prospective financial statement information provides the best estimate of the future financial performance and position of an entity. Readers can then compare actual results against the prospective information.

In our experience, prospective service performance information provides targets and measures for what an entity is aiming to achieve, and this is not necessarily the best estimate of what the entity will achieve. Readers can then compare actual achievements against what the entity aimed to achieve.

This difference suggests to us that the characteristics of prospective financial statement information cannot necessarily be applied to prospective service performance information. We think the proposed amendments could result in unintended changes to the way that prospective service performance information is prepared in future.

In our view the proposed amendments to PBE FRS 42 *Prospective Financial Statements* should not be made. We think the NZASB should carry out further work to determine how best to cater for prospective service performance information.

35. Although we have only had one respondent expressing concerns regarding the amendments to PBE FRS 42, we are aware that Appendix A: *Amendments to Other Standards* contained a number of consequential amendments and there is a risk that respondents did not focus on the proposed amendments to PBE FRS 42.

36. We have given a few examples of the proposed amendments to PBE FRS 42 to help the Board consider this issue. The full set of proposed amendments to PBE FRS 42 is in agenda item 6.5.

**Examples of proposed amendments to PBE FRS 42 (as per limited scope review draft)**

1. The objective of this Standard is to establish principles and specify minimum disclosures for entities that present general purpose prospective financial statements or general purpose prospective service performance information (hereafter referred to as 'prospective financial statements' and 'prospective service performance information' except where otherwise stated). To provide users with high quality general purpose prospective financial information, this Standard requires that an entity presenting general purpose prospective financial information present a complete set of prospective financial statements using the best information that could reasonably be expected to be available and which meet certain qualitative characteristics. This Standard also requires that an entity presenting general purpose prospective service performance information present comprehensive information that is based on the assumptions and information consistent with that used to prepare any prospective financial information.

...

3. An entity shall apply this Standard where it is required, or chooses, to present general purpose prospective financial information or general purpose prospective service performance information.

...

- 27A. An entity's prospective service performance information shall include sufficient information to enable a reader to obtain a broad understanding of the projected service performance of the entity in a manner that is neither misleading nor biased. Consistent with the requirements of PBE FRS XX Service Performance Reporting it shall include contextual information about the entity, an appropriate and meaningful mix of performance measures and/or descriptions and critical judgements made in reporting prospective service performance information that are relevant to an understanding of that information. An entity's prospective service performance information shall be presented in a manner consistent with how the entity expects to report that information in the future.**

- 27B The presentation of prospective service performance information will often involve the selection of a subset of the information that an entity would present in accordance with PBE FRS XX. Differences between the most recently reported service performance information and prospective service performance information may occur due to changes in an entity's activities or the way in which it collects and reports information.**

...

- 51. All significant assumptions underlying prospective financial statements and prospective service performance information shall be disclosed separately and clearly identified in a manner that makes their significance understandable to users. Where possible, assumptions shall be quantified.**

...

- 55. An entity shall disclose:**
- (a) **The bases on which the significant assumptions have been prepared, including the principal sources of information from which they have been derived;**
  - (b) **The extent to which actual events and transactions have been reflected in the prospective financial statements and prospective service performance information;**

- (c) **The factors that may lead to a material difference between information in the prospective financial statements and prospective service performance information, and the actual financial results and service performance reported prepared in future reporting periods; and**
- (d) **The assumptions made in relation to those sources of uncertainty and the potential financial effect of the uncertainty on the prospective financial statements, and the potential effect of the uncertainty on prospective service performance information.**

37. R12 also commented on prospective financial reporting.

**R12's comments:**

The draft states that this Standard does not apply to prospective financial reporting, however a lot of the requirements in here are issues that are best considered when preparing the prospective information rather than the reporting (e.g., type of performance information to use, trade-offs between the characteristics and constraints of performance information, disclosure of judgements etc). I wonder whether there would be benefit in a statement to the extent that where prospective information is prepared, these issues should be considered then rather than in the reporting.

- 38. We agree with R12 that the principles and the factors to consider in the draft standard are relevant both to the preparation of prospective service performance information and the reporting of actual service performance information. This does raise the issue of whether entities preparing prospective service performance information should focus more on these principles and factors, or more on the principles and requirements in PBE FRS 42, or some combination of the two. We note that following changes to legislative requirements in recent years, there may be ongoing changes in practice and that it would be useful to obtain more information about current practice and trends in reporting.
- 39. In light of R6 and R12's comments we recommend that the Board agree not to amend PBE FRS 42 as part of this project. Instead, we recommend that, as suggested by R6, the Board carry out further work to determine how best to cater for prospective service performance information.
- 40. The Board is currently considering amendments to FRS-42 *Prospective Financial Statements*, the for-profit equivalent to PBE FRS 42, with a view to then considering amendments to PBE FRS 42. The Board could consider any amendments to PBE FRS 42 as part of that project. Alternatively, the Board could consider, as a separate piece of work, where requirements for reporting prospective service performance information should be located. Regardless of which alternative the Board prefers, we think there would be merit in separate due process about prospective service performance information so that constituents could focus on those issues.
- 41. If the Board agrees with our recommendation we will need to check the references to PBE FRS 42 in the draft standard and in other standards and rewrite some BC paragraphs.

<p>Q6. Does the Board agree not to proceed with the consequential amendments to PBE FRS 42 as part of this project?</p>
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**Issue 7: Comments on guidance**

42. Quite a few respondents (R3, R4, R5, R7, R9 and R10) noted the importance of the NZASB developing guidance to sit alongside the draft accounting standard. We have therefore provided some background information about the NZASB's project to develop an explanatory guide to support the proposed service performance reporting standard.
43. Table 3 provides a summary of work undertaken by staff and key decisions that have been made to date by the SPR subcommittee and Board in relation to developing guidance.

**Table 3: NZASB Project on an Explanatory Guide for SPR**

Date	Details
Mar 2016 NZASB meeting	The Board provided direction on the development of an explanatory guide to support the proposed standard on service performance reporting.
April–May 2016	At the directive of the Board, staff undertook the following work: <ul style="list-style-type: none"> <li>• Documented existing guidance on reporting service performance information.</li> <li>• Contacted key constituent groups such as central agencies and SOLGM to identify the guidance that is already available in the public sector and seek their views on the development of guidance by the NZASB.</li> <li>• Prepared a paper for the NZASB and NZAuASB SPR subcommittees that summarises the results of the work undertaken.</li> </ul>
7 June 2016 Subcommittee meeting	The subcommittee considered the feedback from key constituent groups in the public sector and examples of existing guidance on reporting service performance information. It also considered the possible structure and content of an explanatory guide.  The subcommittee decided that the focus in the first instance should be developing guidance for not-for-profit entities. The subcommittee felt there was already a level of experience and ability in Tier 1 and 2 of the public sector. The guidance should include examples (looking at different types of organisations) and be focused on Tier 2 not-for-profit entities (i.e. the smaller not-for-profit entities). The subcommittee agreed that the guidance should take the form of a separate explanatory guide. The guidance will not preclude PS organisations from using it, however, it will have an NFP flavour and the examples will be based on NFP organisations. This will be explained in the introduction or foreword to the explanatory guide.
15 Sept 2016	In analysing submissions on the 2016 ED the Board considered feedback on the type of guidance the NZASB should develop. After considering the responses and feedback from its subcommittee the Board agreed that staff should focus first on developing guidance for smaller Tier 2 not-for-profit entities.
Dec 2016 NZASB meeting	The Board considered a first cut of an Explanatory Guide using CPA Canada Guide, <i>Improved Annual Reporting by Not-for-Profit Organizations</i> (2011 publication) and some NZ ideas, the first cut included possible structure and contents as bullet points.



Date	Details
29 June 2017	Staff sent an outline of draft SPR guidance to CPA Canada, to seek approval to use some material from a CPA Canada 2011 publication. CPA Canada has responded favourably, subject to agreeing attribution details.

44. Respondents to the limited scope review draft also made some specific comments in relation to the guidance. Table 4 summarises these comments and indicates the staff response.

**Table 4: 2017 Comments on guidance**

Respondent comment	Staff response
R3 suggested developing guidance/education material to explain the difference in terminology/requirements that we now have between the Tier 3 and Tier 4 and the draft accounting standard.	Agree. The explanatory guide could acknowledge the differences in terminology and explain that the of the terms outputs and outcomes could still be used.
R3 commented that the disclosure of critical judgements is vitally important and suggested that this is an area where practical examples and guidance may be most beneficial.	Agree. We should consider this in the development of the explanatory guide.
R3 suggested it would be beneficial to obtain the views of a range of preparers from the sector to obtain some first-hand feedback of their understanding and interpretation of what the standard is asking from them. Respondent would be happy to assist.	Agree. This could be a useful exercise to identify what areas the guidance should focus on.
R4 suggested that the NZASB work with agencies and auditors in the state sector to pull together a series of examples of “what good looks like”.	Board has agreed at this stage that the focus of an explanatory guide will be on Tier 2 not-for-profit entities. Central agencies usually establish guidance to assist public sector entities to meet their reporting obligations.
R5 suggested providing additional guidance around the factors included in paragraph 19 of the draft standard. Also noted it would be useful to include illustrative examples of where there has been a trade-off between the QCs and the disclosure of critical judgements.	Agree. We should consider these suggestions in the development of the explanatory guide.
R7 commented it is essential to develop sector-appropriate guidance and provide exemplars for both Tier 1 and 2 not-for-profit organisations.	Board has agreed at this stage that the focus of an explanatory guide will be on Tier 2 not-for-profit entities.
R10 commented that although the standard includes some guidance (paragraph 25) on reporting on longer-term social effects of a PBE’s activities, this is an area where	Agree. We should consider this in the development of the explanatory guide.

Respondent comment	Staff response
additional guidance would be useful.	

Q7. Does the Board agree that the focus of the proposed explanatory guide should continue to be Tier 2 not-for-profit entities?

#### Issue 8: Post-implementation review

45. Not surprisingly, given that this will be a new standard on an important topic, some respondents (R4, R6) have proposed that the NZASB conduct a post-implementation review of the standard. We note that this is common practice for major new standards and recommend that the NZASB consider this suggestion when it next reviews its strategic action plan.

Q8. Does the NZASB agree to consider the suggestion for a post-implementation review of this standard when it next reviews its strategic action plan?

#### Issue 9: Differences between the Tiers

46. A number of constituents (R3, R10) commented on the differences between the revised proposals for Tiers 1 and 2 and the requirements for Tiers 3 and 4.

47. The biggest difference is that the Tier 3 and 4 standards refer to outputs and outcomes. This terminology has been dropped in the revised Tier 1 and 2 proposals. Respondents noted the potential for confusion, especially in group situations, but accepted that there was little that could be done about this in the short term. Respondents highlighted the importance of reviewing the Tier 3 and 4 requirements. R3 suggested that some guidance material or education may be of assistance in this area.

48. The Board intends to conduct a post-implementation review of the Tier 3 and 4 standards. This intention is set out in the Board's Strategic Action Plan 2017–2022.<sup>2</sup>

49. Although the draft accounting standard for Tier 1 and 2 entities does not use the terms outputs and outcomes, an entity can still choose to report on outputs and outcomes. These terms were dropped because it became apparent that constituents use the term outcomes in different ways, and because requirements to report on outputs and outcomes have been removed from some public sector legislation. The decisions to focus on principles and drop the more specific requirements in the 2016 ED were to allow for entities reporting under a variety of frameworks, not to stop entities using the terms outputs and outcomes.

Q9. Does the Board agree that differences between tier requirements should be considered in the context of its post-implementation review of the Tier 3 and 4 standards?

<sup>2</sup> Action 1C.2 *Post-implementation Review of Tier 3 and Tier 4 PBE Accounting Requirements*.

## Other issues

50. In this memo we have addressed the issues that we consider require Board discussion.

Q10. Are there any other matters that the Board wants to discuss?

## Recommendations

51. Each recommendation refers to the relevant question(s) for the Board in the memo.
52. We recommend that the Board:
- (a) Q1: PROVIDES FEEDBACK on which of the proposed changes (in agenda item 6.5) to the qualitative characteristics and the disclosure requirements does the NZASB support?
  - (b) Q2: AGREES not to change the scope requirements;
  - (c) Q3: AGREES not to include a definitions section;
  - (d) Q4: AGREES not to change the requirements for disclosure of cost information;
  - (e) Q5: AGREES the standard should have an effective date of 1 January 2021, with early adoption permitted;
  - (f) Q6: AGREES not to proceed with the consequential amendments to PBE FRS 42 as part of this project;
  - (g) Q7: AGREES the focus of the proposed explanatory guide should continue to be Tier 2 not-for-profit entities;
  - (h) Q8: AGREES to consider the suggestion for a post-implementation review of this standard when it next reviews its strategic action plan;
  - (i) Q9: AGREES that differences between tier requirements should be considered in the context of its post-implementation review of the Tier 3 and 4 standards; and
  - (j) Q10: PROVIDES feedback on any other matters.

## Next steps

53. We will revise the draft accounting standard to reflect the feedback from this meeting and plan to seek approval to issue the standard in November.
54. We propose the following agenda papers for the November meeting:
- (a) Cover memo;
  - (b) Due process memo;
  - (c) Draft standard (revised to reflect decisions from this meeting);<sup>3</sup>
  - (d) Signing memo; and
  - (e) Revised feedback statement.

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<sup>3</sup> We will need to do further work on the consequential amendments and Basis for Conclusions to reflect decisions from this meeting. We will also remove the Tables of Concordance from the draft standard.

55. We propose to develop a feedback statement based on that issued in May 2017, together with an additional column to identify any significant changes made in finalising the standard (as shown below).

Proposals in the 2016 ED	What we heard	What we changed (as at May 2017)	Final standard (issued Date)

## Attachments

- Agenda item 6.3: Analysis of submissions received
- Agenda item 6.4: Submissions received (in supporting papers)
- Agenda item 6.5: Draft PBE FRS XX Service Performance Reporting
- Agenda item 6.6: Letter to constituents: May 2017 (in supporting papers)
- Agenda item 6.7: Feedback Statement on 2016 ED (in supporting papers)
- Agenda item 6.8: The accountability information needs of key charity funders (in supporting papers)<sup>4</sup>

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<sup>4</sup> This article accompanied R7's submission.

## Service Performance Reporting

### Analysis of submissions on limited scope review draft

This document contains the comments made by respondents, together with a staff response.

If the staff response says “see issue x in the memo” the matter is discussed in agenda item 6.2.

Once we have worked through the issues in agenda item 6.2, we will ask if the Board wants to raise any other issues.

R#	Comment	Staff response
R1	<p>The greatest area of concern for me is what happens with tier 1/2 charities which have consolidated entities under the control rules, will they need to consolidate results? If so there will be double counting.</p> <p>In our case we have:</p> <ol style="list-style-type: none"> <li>1. Inc Society (Tier 2) who consolidates all entities below</li> <li>2. Company (Tier 2) who consolidates all entities below</li> <li>3. 30 Charitable Trusts + 1 company (All tier 3)</li> </ol> <p>In our case for the top entity would we need to consolidate the results for the entities below, if so the results from the 30 charitable trusts will effectively be triple counted.</p>	<p>Paragraph 11 of the draft standard states that except as otherwise required by legislation, an entity shall present service performance information for the same reporting entity and reporting period as the financial statements.</p> <p>No change to draft standard.</p> <p>Each reporting entity will need to decide what to report. The cross-referencing provisions may assist if entities think that there would be unnecessary duplication of information.</p>
R2	<p>Thank you for the opportunity to comment on the limited scope consultation on the above Standard. I believe the Standard in its current form captures the current best practice of performance reporting. It also allows for new forms of reporting to develop to enable Public Benefit Entities (PBEs) to communicate better their performance to users.</p>	<p>Support noted.</p>
R2	<p>I would encourage all PBEs to report under this standard as soon as is practicable. I recognise that the NZASB has weighed the costs and benefits of an early mandatory adoption to decide on the January 2021 implementation date, but would prefer to see a two year instead of three year transition period. This will raise the quality of reporting much more quickly and increase its comparability as well. Two pieces of research I am involved in inform this view.</p>	<p>See Issue 5 <i>Effective date</i> in agenda item 6.2.</p>

R#	Comment	Staff response
	<ol style="list-style-type: none"> <li>1. Completed cross-jurisdictional research with Danielle McConville from Queens University Belfast where we analysed one year's reporting from matched charities in Australia, New Zealand, the UK and US. It shows that under UK mandatory performance reporting, charities report more in the way of outputs, outcomes (societal and individual) and 'bad news', as well as provide more information to allow these data to be verified (i.e. explanations of how different measures were calculated). And the UK requirement is simply for charities to report on the public benefit they deliver (and the SORP's encouragement for larger charities to 'consider the difference they have made in reference to terms such as inputs activities, outputs, outcomes and impacts'). This encouragement makes a real difference to reporting.</li> <li>2. Ongoing research being conducted with Janet Mack and Stuart Tooley from QUT in Brisbane considering three years of data from matched charities in Australia, New Zealand and the UK. Preliminary findings suggest that, due to a lack of guidance, entities change the way they make narrative disclosures about volunteers year-on-year. There also appears to be no effort to standardise across the same entity in the three jurisdictions. Comparability is therefore lacking, making it difficult for GPFR users to really understand entities' performance. While comparability is already difficult in the performance reporting arena, it is necessary to encourage PBEs to use qualitative characteristics consistently to increase this reporting's usefulness.</li> </ol>	<p>Acknowledge the comments about difficulty of obtaining comparability between entities. The draft standard does include some requirements about consistency over time. Paragraph 40 states that an entity shall report service performance consistently. If an entity changes what it reports or how it reports its service performance information, it shall explain the nature of those changes and their effect on the current period's service performance information.</p>
R2	<p>I also suggest a minor wording change to the last sentence of paragraph 25 to match the ideas in the prior sentences. It could be changed to read: 'Examples of broad or longer-term effects include changes to these individuals' and groups' educational achievements or health, or changes to groups' or societal poverty or crime levels.'</p>	<p>Agree with editorial suggestion. Shown as mark up in draft standard (agenda item 6.5).</p>
R2	<p>Congratulations on the Standard, the Introduction and Basis for Conclusions which I believe spell out the need for this reporting and will assist PBEs to communicate their story to their users.</p>	<p>Support noted</p>

R#	Comment	Staff response
R3	<p><b>Background context regarding Service Performance Reporting</b></p> <p>Our views in this and our earlier submission have been formed largely from our direct involvement in assisting clients and other stakeholders individually and in groups in matters relating to service performance reporting. This has included providing education regarding service reporting via seminars, workshops and article writing. We have also been involved in assisting clients with the preparation of service performance reports as well as providing assurance over early adopters and Tier 3 entities' performance reports.</p>	<p>Noted. Not sure what the respondent means by "early adopters". We are aware that some NFPs have decided to report service performance information in advance of a standard.</p>
R3	<p><b>Overarching Observations</b></p> <p>We strongly agree with the overall aim of requiring entity and service performance reporting and applaud the New Zealand developments in this area. Our view is that a more holistic level of performance reporting that this initiative will engender should be a very positive development for stakeholders seeking information about PBEs in New Zealand, and more generally for New Zealand society.</p> <p>We believe service performance information should provide much more useful information for stakeholders and decision makers who in most cases do not have the power to require such information. Due to the service objectives of most PBEs we believe the information required by service performance reporting is generally much more important for assessing an entity's overall performance than just the financial statements.</p> <p>We also note the strong parallels with the international movement towards requiring integrated reporting. As such, with the legislative requirement already in place in New Zealand for entity information and service performance reporting applying to some PBEs, we believe New Zealand has the opportunity to be an international leader and role model in this area.</p> <p>However, while we see this as a significant opportunity to improve reporting in New Zealand for PBEs, we also do not underestimate the challenge that this new requirement will impose of some entities. From our experience with assisting clients to date we have found vastly differing levels of ability, and desire, to provide service performance reporting. This is in terms of the buy-in to the concept at the governance level, understanding the technical requirements, resources and capacity constraints within organisations, as well as whether the type of activities of the specific PBE lend themselves</p>	<p>Support for developing a standard noted.</p>

R#	Comment	Staff response
	<p>to ease of service performance reporting (e.g. where outputs and outcomes are not easily definable or attributed to a single entity in a multi-entity environment).</p> <p>We have also already experienced first-hand the difficult situation auditors can be placed in when they are having to educate clients about the requirements for service performance reporting where client and/or their external accountant's awareness and knowledge is sadly lacking. Accordingly, we support all efforts in raising awareness and promoting education for preparers and auditors. It is important that these initiatives also target governing bodies as their early engagement and buy-in to the concept is critical in ensuring that meaningful information is produced and reported. We have been urging philanthropic funders who we are in contact with to assist in this area in relation to assisting preparers, as good quality service performance reporting is in their best interests as well as being positive for the wider community.</p> <p>Having said this, we have on the whole been impressed with how well many of the Tier 3 &amp; 4 entities we deal with have quickly grasped the service reporting concept and made good initial attempts at their service reporting. A further observation is that entities themselves have been better at doing this than some chartered accountants assisting small charities in their reporting, i.e. the level of knowledge of the chartered accountants in some cases has been embarrassingly lacking.</p> <p>As regards auditors, we believe it is important that they are given the tools and education to assist their clients, and especially so as not to squash this early stage initiative with a rigid overly strict compliance attitude. Specifically, we see the scenario that a plethora of qualified audit opinions, a possible outcome of risk adverse auditors, would likely be very detrimental to this emerging area.</p> <p>Hence, we suggest considerable care needs to be taken to strike an appropriate balance between requiring achievable information and not making this so hard to produce and audit that it causes bad-will and negates the positive intention. Failure for this new reporting to be embraced positively by the sector will result in information of much less use to wider stakeholders, and likely criticism of it being seen as a further compliance cost.</p>	



R#	Comment	Staff response
R3	<p><b>Your Question</b></p> <p>Overall we believe that the decision to move to a higher principle based approach to be a sensible one. We expect that this greater flexibility in how to tell their story will be appreciated by preparers and the wider sector. In addition, we hope that this will encourage a positive reaction from the sector to this new requirement as well as greater innovation in reporting and communication to stakeholders.</p> <p>We have the following main concerns with the revised proposed accounting standard.</p>	Overall support for principles-based standard noted.
R3	<p><b>Timing</b></p> <p>We are concerned in relation to the likely effective date of the proposed service performance accounting standard. We understand this is proposed to be effective for periods beginning on or after 1 January 2021 (i.e. December 2021 year-ends). While we appreciate the logistics challenge of approval of a new standard, and the need to allow some implementation readiness period, we are concerned that some in the sector are likely to see this not needing to do anything until 2021. We believe this will be a lost opportunity for significantly improved reporting in the PBE sector.</p> <p>We appreciate that early adoption before the mandatory date will be available once the standard is issued. However, our past experience of accounting standard changes would indicate that only a few are likely to voluntarily early adopt. We think that a mandatory date that far out will be a significant lost opportunity to substantially improve the quality of PBE reporting in New Zealand. We have already seen some significant positive in improved stakeholder communication, clearer organisational focus, and a positive response from many funders to the Tier 3 and 4 PBE requirement for service performance reporting.</p> <p>We also understand that one of the logistics concerns is the desire to ensure that the new SSP standard and the related SSP assurance standard are effective at the same time. If this is the primary hold-up for earlier implementation we do not believe that it would be a significant problem if the SSP element of Tier 1 and 2 PBEs was not required to be audited for say 1 year. However we appreciate that this may have legislative challenges.</p>	See Issue 5 <i>Effective date</i> in agenda item 6.2.

R#	Comment	Staff response
R3	<p><b>Difference in terminology from the Tier 3 &amp; Tier 4 requirements</b></p> <p>While we appreciate the rationale to take the proposed accounting standard to a higher principles basis, we believe it is unfortunate that the terminology is now inconsistent between the proposed Tier 1&amp;2 requirements and the Tier3&amp;4 standards. This is with the latter still referring to the terms Outcomes and Outputs. We also note subtle differences in the fundamental questions that the two standards are asking of preparers to answer.</p> <p>We have already experienced some client confusion around service performance terminology and requirements when assisting a Tier 2 entity thinking about their own service performance reporting in the context of them assisting their Tier 3 subsidiary entities with outputs ad outcome reporting.</p> <p>We expect a possible unintended consequence could arise from a Tier 1 or 2 PBE trying to report on an outputs and outcomes basis by consolidating the service performance reports of multiple subsidiaries.</p> <p>We appreciate that the NZASB is unlikely to want to disrupt the Tier 3 &amp; 4 standards so soon after their issue and hence we are likely to just have to live with this situation. As such we suggest that some guidance material or education may be of assistance in this area.</p>	<p>See agenda item 6.2  <i>Issue 9 Difference between Tiers</i>  <i>Issue 7 Comments on guidance</i></p>
R3	<p><b>Specificity of requirements from an audit perspective</b></p> <p>We believe that the revised accounting standard may pose some challenges to auditors due to the very high level principles approach and the lack of strict defined criteria or a generally understood and agreed framework for auditors to assess reporting against. For example, it may be more challenging for the auditor to determine material omission of information (e.g. particularly where the entity's performance has not been positive). Without clear requirements or guidance within the accounting standard this may result in auditors being put in the difficult position of being unhappy with disclosure when the preparer may feel there is no compulsion to disclose from their interpretation of the accounting standard that they are following.</p> <p>On balance we believe that this is probably just a price to pay for a high-level accounting standard in an area that is by its nature more subjective and varied than areas normally covered by accounting standards. However, it is probably better that such a challenge is</p>	<p>See Issue 1 <i>Subcommittee issues (QCs and disclosures)</i> in agenda item 6.2 and consider feedback from joint subcommittee meeting held on 5 September 2017.</p> <p>Background information          (from previous reporting back to subcommittees on comments raised by NZAuASB)</p> <p>The NZASB does not plan to develop additional guidance on materiality in relation to service performance. Entities have to apply the QCs,</p>

R#	Comment	Staff response
	<p>given to the likely smaller population of qualified auditors, rather than a greater challenge being imposed over the larger, and possibly not always as technical accounting skilled (?), preparer population.</p> <p>We do however see the requirement for preparers to disclose their critical judgements as regards service performance reporting to be vitally important in order to allow auditors to perform their work and to avoid unnecessary qualified audit opinions. We also believe some description of how materiality has been applied by preparers may also be required.</p> <p>We appreciate the explanation of judgements to be disclosed in paragraphs 45 and 46 of the proposed standard and consider these helpful explanations. However, we have a remaining concern as to how the term “critical” will be interpreted by preparers and fear this may be open to potentially very wide interpretation by different preparers. Our concern primarily with this term is that some may take it as being a negative interpretation and hence may not be inclined to disclose otherwise important or significant information as they don’t assess this as critical. Accordingly, we think this area is one where practical examples and guidance may be most beneficial.</p> <p>A further consequence or trade-off, is that the greater flexibility allowed to preparers will likely lead to reduction in comparability between entities operating in similar fields. This may also reflect different interpretations by different auditors as to what is acceptable under the standard. In an extreme case, this could raise the risk of auditor opinion-shopping.</p> <p>We suggest consideration be given to any guidance an education to assist preparers with judgement disclosure. We also urge guidance and education be developed to auditors regarding how to approach the audit of this new and in some cases, challenging area of reporting.</p>	<p>with relevance being a driver of what to report and neutrality requiring both the good and bad news. (refer to the principles section in the draft standard and reminders in paragraphs 21 and 22 in the information to be reported section).</p> <p>The proposed amendments to PBE IPSAS 1 (see paragraphs 46A.1 and 46A.2) might address some of these concerns.</p> <p>Paragraph 46A.1 notes that materiality has an important role in guiding the selection of service performance information to report.</p> <p>Paragraph 46A.2 lists matters for consideration when making judgements about whether items of service performance are material.</p> <p>Also see Issue 7 <i>Comments on guidance</i> in agenda item 6.2.</p>
R3	<p><b>Guidance</b></p> <p>As noted above we believe that good practical guidance will be required if this important new standard is to be positively received and adopted and the benefits from this improved stakeholder communication is to be realised. Given the nature of the standard’s subject matter we think it may be very beneficial to obtain the views of a range of preparers from the sector to obtain some first-hand feedback on their understanding and</p>	<p>See Issue 7 <i>Comments on guidance</i> in agenda item 6.2.</p>

R#	Comment	Staff response
	interpretation of what the standard is asking of them. We would be happy to assist in facilitating this if of value.	
R4	<p>We thank the NZASB for revising the Service Performance Reporting standard to reflect feedback from submissions on Exposure Draft 2016-6.</p> <p>The Treasury doesn't have additional comments on the workability of the revised proposals. Having a standard for service performance information is a significant new development and it has been a long-awaited initiative for the public sector. It is therefore expected that lessons will be learned on how to apply this principles-based standard in the first couple of years of implementation. We believe that best practice will develop over time as entities come to grips with the requirements. We encourage the NZASB to schedule a post-implementation review to pick up lessons learnt, check that the standard is operating as intended and determine what, if any, changes may be needed to the standard.</p> <p>We understand that a complementary Auditing Standard for Service Performance Reporting is currently being drafted. We believe it is critically important that this standard reinforces the flexibility available to agencies to report their service performance in the most appropriate way.</p> <p>The application of the Auditing Standard will also be important as we do receive feedback from agencies that a focus on quantitative measures by auditors can be a barrier to providing service performance information that is useful for accountability and decision making purposes.</p> <p>The Guidance, to be issued by the NZASB to assist with implementation of the Service Performance Reporting standard, is an opportunity to demonstrate the flexibility available to agencies to report their information in the way that best demonstrates the value that has been created through the delivery of a particular service./ We often hear from agencies that they want examples of "what good looks like: and we encourage the NZASB to work with agencies and auditors to pull together a series of examples. We suggest that this guidance be updated as good examples emerge from application of the standard.</p>	<p>See Issue 8 <i>Post implementation review</i> in agenda item 6.2.</p> <p>Note when discussing feedback from joint subcommittee meeting to be held on 5 September 2017.</p> <p>See Issue 7 <i>Comments on guidance</i> in agenda item 6.2. The NZASB has previously agreed to focus on smaller not-for profit Tier 2 entities rather than all entities.</p>

R#	Comment	Staff response
	We look forward to continuing to work alongside the NZASB to achieve better service performance reporting in the State sector.	
R5	<p>Thank you for your letter dated 29 May and the opportunity to provide feedback on the limited scope review draft of the Service Performance Reporting standard (the “draft standard”). Service performance reporting is becoming increasingly prevalent, and we commend the New Zealand Accounting Standards Board’s (NZASB) efforts to establish a framework for such reporting in New Zealand. We acknowledge that the proposals have undergone significant revision and are now very different to Exposure Draft 2016-6 (“the ED”). We consider that, on the whole, the changes made reflect the views expressed in our submission on the ED as well as those conveyed by other parties.</p> <p>We appreciate the difficulty in developing a standard which will apply to both the public sector and the not-for-profit (NFP) sector. There are a number of different service performance reporting requirements across these sectors, including those written into legislation and those set by funders. As such it is important to avoid introducing conflicting or potentially confusing requirements in the draft standard. We support the high-level principles-based approach taken in the draft standard to allow both public sector and NFP entities the flexibility to report service performance information in accordance with any existing requirements.</p> <p>We welcome the flexibility encouraged by the draft standard and the fact that it does not prescribe the format of service performance information. Such flexibility will encourage entities to ‘tell their performance story’ in a way that is appropriate for that entity and as such will better meet user’s needs. The ability to report more specific information also aligns with one of the International Accounting Standards Board’s (IASB) key themes; <i>Better Communication in Financial Reporting</i>.</p> <p>Against this backdrop of support, we have the following comments.</p>	Support for increased flexibility noted.

R#	Comment	Staff response
R5	<p><b>Scope</b></p> <p>Paragraph 3(b) refers to “<i>Tier 1 and Tier 2 public sector public benefit entities required by legislation to provide information in respect of service performance in accordance with generally accepted accounting practice (GAAP)</i>”. The reference to GAAP will scope out some entities where legislation does not explicitly reference GAAP such as council-controlled organisations under section 68 of the Local Government Act 2002 and school board’s under section 87 of the Education Act 1989. On this basis we recommend removing the reference to GAAP so that all Tier 1 and Tier 2 public sector public benefit entities required by legislation to provide information in respect of service performance must do so in accordance with the standard.</p>	<p>See Issue 2 <i>Scope</i> in agenda item 6.2.</p> <p>We propose no change in response to this comment. The reference to GAAP was a deliberate addition following consideration of respondents’ comments on the 2016 ED.</p>
R5	<p><b>Qualitative characteristics</b></p> <p>The flexibility permitted by the draft standard gives rise to the risk of biased reporting of service performance information. Paragraph 8 acknowledges that “<i>all qualitative characteristics may not be fully achieved, and a balance or trade-off between certain of them may be necessary</i>”. In our view the qualitative characteristic of ‘<i>faithful representation</i>’ is paramount – service performance information should always be complete, neutral and free from material error. Therefore we recommend that no trade-off be permitted for this qualitative characteristic.</p>	<p>We propose no change in response to this comment. The wording comes directly from the PBE Conceptual Framework (paragraph 3.4). The PBE Conceptual Framework is based on the IPSASB’s Conceptual Framework which, unlike the IASB’s Conceptual Framework, does not distinguish between fundamental and enhancing QCs.</p> <p>3.4 Each of the qualitative characteristics is integral to, and works with, the other characteristics to provide in GPFRs information useful for achieving the objectives of financial reporting. However, in practice, all qualitative characteristics may not be fully achieved, and a balance or trade-off between certain of them may be necessary.</p> <p>The draft standard contains a list of all the QCs, along with a brief explanation.</p>

R#	Comment	Staff response
R5	<p><b>Disclosure of judgements</b></p> <p>The requirement to disclose critical judgements in paragraph 44 is essential as it provides the criteria for an assurance practitioner to evaluate the reported service performance information against when conducting an assurance engagement. These criteria also need to be available to the intended users to allow them to understand how decisions are made on what is reported and why. Therefore, we would be concerned if the requirement to disclose critical judgements was removed as a result of this limited scope consultation.</p>	<p>Support for disclosure of critical judgements noted.</p> <p>See Issue 1 <i>Subcommittee issues (QCs and disclosures)</i> in agenda item 6.2.</p>
R5	<p><b>Guidance and illustrative examples</b></p> <p>Reviews of Tier 3 and 4 charity Performance Reports have highlighted the challenges experienced in meeting the new reporting requirements for service performance information. Similar transitional issues were experienced when the public sector adopted service performance reporting two decades ago. As such, additional guidance would be well received. The factors included in paragraph 19 are a good starting point in this regard. In particular it would be useful to include an illustrative example where there has been a trade-off between the qualitative characteristics. Given its importance, we also recommend illustrative examples of disclosures of critical judgements.</p>	<p>See Issue 7 <i>Comments on guidance</i> in agenda item 6.2.</p> <p>The Board has not planned to develop illustrative examples to accompany this standard. Given the range of entities that will be applying the standard this would be a difficult exercise and create a number of risks. It would also defer completion of the project.</p> <p>We plan to develop an explanatory guide to assist smaller Tier 2 NFPs.</p>
R5	<p><b>Structure</b></p> <p>The format of the PBE Standards generally include a 'Definition' section after the 'Scope' section. For consistency, we recommend inclusion of a 'Definition' section where the terms '<i>service performance information</i>' and '<i>appropriate and meaningful</i>' are explicitly defined. We note that '<i>service performance information</i>' has been described in paragraph 2 and this could form the basis for the definition. We also note that paragraph BC21 clarifies that the term '<i>appropriate and meaningful</i>' should be considered from the user's point of view. Paragraph 22 also provides discussion on assessing which performance measures are the most appropriate and meaningful. Both of these could be drawn upon in the development of a definition.</p>	<p>See Issue 3 <i>Structure/Definitions</i> in agenda item 6.2.</p> <p>We propose no change in respect of this comment.</p>

R#	Comment	Staff response
R5	<p><b>Trans-Tasman alignment</b></p> <p>We note the Australian Accounting Standards Board (AASB) is also working on an accounting standard for reporting service performance information and has been working closely with the NZASB in developing the proposals. We encourage trans-Tasman harmonisation, where appropriate, in finalising the requirements of these standards.</p>	<p>Desire for trans-Tasman alignment noted.</p> <p>AASB Work Program (as at 17 August 2017) does not indicate a target date for completion of its SPR project.</p>
R5	<p><b>Appendix A Editorial Suggestions</b></p> <p>Paragraph 6</p> <p>Insert '<i>holistic</i>' (ie 'Presentation of service performance information together with financial statements enables users to make [<i>holistic</i>] assessments of the entity's performance').</p> <p>6. An entity shall present service performance information that is useful for accountability and decision-making purposes in the same general purpose financial report as its financial statements. Presentation of service performance information together with financial statements enables users to make assessments of the entity's performance.</p>	<p>We propose no change in respect of this comment.</p> <p>If the Board would like to change this sentence we would suggest "make <i>more complete</i> assessments...". This would then tie in with paragraph BC7.</p> <p>Paragraph BC7 states that "The provision of service performance information, together with financial statements, provides users with a more complete set of information."</p>
R5	<p>Paragraph 14</p> <p>Change '<i>often</i>' to '<i>should</i>' (ie 'However, public benefit entities [<i>should</i>] have long-term service performance objectives'). Paragraph 15(a) requires entities to report contextual information about what it intends to achieve over the medium to long term so the proposed terminology appears to be inconsistent with this requirement.</p> <p>14. This Standard establishes requirements for reporting on an entity's service performance for a reporting period. However, public benefit entities often have long-term service performance objectives. Judgement is required in deciding how much information to provide about the entity's service performance in the current reporting period and how much information to provide about progress towards its long-term objectives. In reporting on its current period's service performance an entity is likely to need to provide information that relates to previous periods or future periods (such as trend data) to provide context.</p>	<p>We propose no change in respect of this comment.</p> <p>The requirement in paragraph 15(a) was deliberately worded very broadly. We have tried to avoid commenting on how an organisation should be managed and, in particular, have been careful to avoid the suggestion that an entity must have specific objectives.</p>



R#	Comment	Staff response
R5	<p>Paragraph 17</p> <p>Delete '<i>at its highest level of management or in the governance of the entity</i>' and the second mention of '<i>performance framework, theory of change or intervention logic</i>'</p> <p>We consider these references are superfluous and make the paragraph difficult to read</p> <p>17. Paragraph 15(a) requires contextual information about why an entity exists, what it intends to achieve and how it goes about this. This information should be drawn from relevant documents such as founding documents, governance documents, accountability documents and planning documents. For example, a not-for-profit entity would consider documents such as its constitution, trust deed, mission statement (vision, purpose) and its most recent plans and strategies. If an entity uses a performance framework, theory of change or intervention logic at its highest level of management or in the governance of the entity, the contextual information should also draw upon that performance framework, theory of change or intervention logic. For example, a local authority's Long-Term Plan provides a meaningful performance framework for its activities.</p>	<p>We propose no change in respect of this comment.</p> <p>We agree that the paragraph is a bit wordy. However, the Board was trying to acknowledge the range of documents or frameworks that might be used in practice.</p> <p>If the Board wants to change para 17, the second reference could read "performance framework etc".</p>
R5	<p>Paragraph 20</p> <p>Given the importance of the first sentence we support this being a black letter requirement.</p> <p>20. In reporting on what an entity has done during the reporting period an entity shall provide users with an appropriate and meaningful mix of performance measures and/or descriptions for the reporting period. The performance measures and/or descriptions used by an entity to communicate its service performance may be:</p> <p>(a) Quantitative measures: Examples of quantitative measures are the quantity of goods and services, the cost of goods and services, the time taken to provide goods and services, levels of satisfaction using a rating scale on a questionnaire or survey, and numerical measures for service performance objectives or goals;</p> <p>(b) Qualitative measures: Examples of qualitative measures are descriptors such as compliance or non-compliance with a quality standard, ratings such as high, medium or low, or ratings assigned by experts; or</p>	<p>Agree.</p> <p>R6 made the same suggestion.</p> <p>Bolding added in the draft standard (agenda item 6.5).</p>

R#	Comment	Staff response
	<p>(c) Qualitative descriptions: Examples of qualitative descriptions are those based on participant observations, open-ended questions on interviews and surveys and case studies. For example, how did an entity's service performance activities change the well-being and circumstances of a client group?</p>	
R5	<p>Paragraph 28</p> <p>Given the importance of the sentence 'If an entity reports on the cost of goods and services it shall provide a reconciliation between the expenses in the financial statements and the total goods and services costs reported in the service performance information' we support this being a black letter requirement.</p> <p>28. Reporting on the cost of goods and services provides an important link between the financial statements and service performance information. However, it may not always be practicable, or the most appropriate way of reporting on goods and services. The reporting on the cost of goods and services will depend on an entity's accounting policies and its cost allocation policies. If an entity reports on the cost of goods and services it shall provide a reconciliation between the expenses in the financial statements and the total goods and services costs reported in the service performance information. Where unrecognised goods or services in-kind are a significant component of producing goods and services, any cost information provided shall also acknowledge the use of these resources. PBE IPSAS 23 <i>Revenue from Non-Exchange Transactions</i> establishes requirements for the recognition of donated goods and services.</p>	<p>See Issue 4 <i>Cost of goods and services</i> in agenda item 6.2.</p> <p>We are proposing no change to paragraph 28.</p> <p>We do not think it is appropriate to present paragraph 28 in bold text; not all entities will report on the cost of the goods and services.</p>
R5	<p>Paragraph 32</p> <p>Replace 'An entity may' with 'Where possible an entity shall'</p> <p>32. An entity may cross reference the service performance information and the financial statements so that users can assess the service performance information within the context of the financial statements.</p>	<p>We propose no change in respect of this comment.</p> <p>Paragraph 53 of the 2016 ED was as follows:</p> <p>An entity should include cross references between the service performance information and the financial statements so that users can</p>

R#	Comment	Staff response
		<p>assess the service performance information within the context of the financial statements.</p> <p>The Board agreed to change the wording in this paragraph to “may” as the draft standard does not mandate the reporting on cost of the goods and services and so it was considered inconsistent to have a “should” in this paragraph.</p>
R5	<p>Paragraph BC5</p> <p>Insert ‘to’ (ie ‘in order [to] address a gap in its PBE Standards’).</p> <p>BC5. The NZASB issued this Standard to establish requirements for the reporting of service performance information in order address a gap in its PBE Standards and to better meet the information needs of users of general purpose financial reports.</p>	<p>Agree</p> <p>Shown as mark up in the draft standard (agenda item 6.5).</p>
R6	<p>We appreciate the opportunity to comment on Review Draft – PBE FRS XX <i>Service Performance Reporting</i> (the review draft).</p> <p>Overall, we are pleased with the review draft. We think the review draft addresses many of the comments we made in our submission to the External Reporting Board (XRB), dated 28 July 2016, about Exposure Draft NZASB 2016-6 <i>Service Performance Reporting</i>.</p> <p>As requested, we have considered whether the review draft is workable and whether it creates any unintended consequences. At a high-level, other than the proposed amendments to PBE FRS 42 <i>Prospective Financial Statements</i>, we think the review draft is workable and does not create any unintended consequences. We have some concerns about the proposed amendments to PBE FRS 42 <i>Prospective Financial Statements</i> because, in our experience, prospective service performance information is different to prospective financial statement information. We do not think that amending PBE FRS 42 <i>Prospective Financial Statements</i> as proposed, is the best approach to address matters relating to prospective service performance information.</p> <p>We attach to this letter comments about the proposed amendments to PBE FRS 42 <i>Prospective Financial Statements</i> and comments about the review draft that focus on</p>	

R#	Comment	Staff response
	<p>improving some requirements and making some points clearer. Please note that our comments primarily focus on PBEs in the public sector.</p> <p>We see real value in the NZASB conducting a post-implementation review once the standard has been applied in practice for two or three years.</p> <p>Our comments on the review draft and the proposed amendments to PBE FRS 42 <i>Prospective Financial Statements</i> are a result of collaboration between my staff at Audit New Zealand and the Office of the Auditor-General.</p> <p>If you have any questions about our submission, please phone Todd Beardsworth, Assistant Auditor-General, Accounting and Auditing Policy on 021 244 0727 or email him at todd.beardsworth@oag.govt.nz.</p>	<p>Noted. See Issue 8 <i>Post-implementation review</i> in agenda item 6.2.</p>
R6	<p><b>Consequential amendments to PBE FRS 42 <i>Prospective Financial Statements</i></b></p> <p>Prospective service performance information is different to prospective financial statement information.</p> <p>Prospective financial statement information provides the best estimate of the future financial performance and position of an entity. Readers can then compare actual results against the prospective information.</p> <p>In our experience, prospective service performance information provides targets and measures for what an entity is aiming to achieve, and this is not necessarily the best estimate of what the entity will achieve. Readers can then compare actual achievements against what the entity aimed to achieve.</p> <p>This difference suggests to us that the characteristics of prospective financial statement information cannot necessarily be applied to prospective service performance information. We think the proposed amendments could result in unintended changes to the way that prospective service performance information is prepared in future.</p> <p>In our view the proposed amendments to PBE FRS 42 <i>Prospective Financial Statements</i> should not be made. We think the NZASB should carry out further work to determine how best to cater for prospective service performance information.</p>	<p>See Issue 6 <i>Amendments to PBE FRS 42</i> in agenda item 6.2.</p> <p>We agree that this is a significant issue.</p>

R#	Comment	Staff response
R6	<p><b>Output cost disclosure (paragraph 28)</b></p> <p>It is important that performance information is integrated with financial information as set out in paragraph 28 of the review draft. We do not think there will be many situations where it is not practicable for entities to disclose output costs. We think that the bar for non-disclosure of output cost information should be set at a high level. Therefore, we consider that the wording of the review draft should be strengthened to <u>require</u> cost disclosure related to services or activities, unless it is impracticable to do so.</p>	<p>See Issue 4 <i>Cost of goods and services</i> in agenda item 6.2.</p>
R6	<p><b>Cross referencing performance reporting information (paragraph 35)</b></p> <p>Where cross-referenced material forms part of the service performance report for a particular period, we think that information should be required to remain <u>static</u> as well as available. We would be concerned if cross referenced information was updated over time and the historical information lost.</p> <p>(We are less concerned about cross referenced information that does not make up the service performance report.)</p>	<p>Agree.</p> <p>Proposed changes shown in mark up in the draft standard (agenda item 6.5).</p>
R6	<p><b>Material prior period errors (paragraph 43)</b></p> <p>Paragraph 43 could be improved by stating that material numerical prior period errors should be corrected <u>and</u> accompanied by a narrative explanation of the error.</p> <p>We are happy that narrative prior period errors are required to be explained.</p>	<p>Agree.</p> <p>Proposed changes shown in mark up in the draft standard (agenda item 6.5).</p>
R6	<p><b>Disclosure of judgements (paragraphs 44–46)</b></p> <p>Paragraph 45 defines critical judgements as “those that have the most significant effect on the selection and aggregation of service performance information”. We believe that there are other critical judgments that should be disclosed, such as critical judgements in determining the actual level of performance against a measure.</p> <p>At times we see important performance measures that are challenging to measure, with complex methodologies and key judgements made in applying these. Examples might be:</p> <ul style="list-style-type: none"> <li>• Measuring savings or economic benefits from a major project or initiative,</li> <li>• Quantifying social benefits,</li> </ul>	<p>See Issue 1 <i>Subcommittee issues (QCs and disclosures)</i> in agenda item 6.2.</p> <p>Proposed changes shown in mark up in the draft standard (agenda item 6.5).</p>

R#	Comment	Staff response
	<ul style="list-style-type: none"> <li>Measuring greenhouse gas emissions at an entity or national level.</li> </ul> <p>For these types of measures, we consider some level of disclosure about judgements made in measuring performance (plus perhaps methodologies and assumptions) is important to provide information to the reader about how performance has been assessed.</p> <p>In the public sector critical judgements about selection and aggregation of performance measures are often set out in forward looking documents, such as statements of intent, statements of performance expectations or council long-term plans. We think paragraphs 44 to 46 should make it clear that aspects of the disclosure requirement could be satisfied by cross-referencing to such documents.</p>	
R6	<p><b>Less significant matters</b></p> <p>Paragraph 20 – Paragraph 15 tells users of the review draft “what” information they should provide about service performance, and the text is bold. Paragraph 20 tells users “how” they might measure the information referred to in paragraph 15, and we consider it would be useful and consistent to present paragraph 20 in bold text.</p>	<p>Agree.</p> <p>R5 made the same suggestion.</p> <p>Bolding added in the draft standard (agenda item 6.5).</p>
R6	<p>Paragraph 21 – The term “financial statements” should be replaced with “financial report” so it is consistent with other paragraphs in the review draft.</p>	<p>Agree</p> <p>Shown in mark up in the draft standard (agenda item 6.5).</p>
R7	<p>Thank you for providing the opportunity to further comment on the revised proposal that is relevant for Tier 1 and Tier 2 public benefit entities service performance reporting.</p> <p>Overall, I am supportive of the New Zealand Accounting Standard Board’s revised proposal. I am also pleased to find some significant changes made to the 2016 Exposure Draft. In order to assist the collation and analysis of comments, a XRB template is followed to provide specific comments regarding the workability of the revised proposal. Sector-appropriate guidance and exemplars are suggested to be developed in order to avoid confusion in applying this revised proposal.</p> <p>Please note that my comments focus specifically on Tier 1 and Tier 2 not-for-profit, rather than public sector public benefit entities. The views expressed in this submission are my</p>	<p>Note overall support</p>

R#	Comment	Staff response
	<p>own personal views and do not necessarily reflect the views of Auckland University of Technology.</p> <p>Should you wish to discuss any matter below, please do not hesitate to contact me.</p> <p>***</p> <p><i>R7 also included a copy of the table in the feedback statement and commented on each of the changes identified in the feedback table. R7's comments on each row in the feedback statement are shown below.</i></p>	
R7	<p><b>Objective</b></p> <p>Agree</p>	Noted
R7	<p><b>Accountability and Decision Making</b></p> <p><i>Introduction</i></p> <p>The inclusion of an introduction provides an overview of the standard. The current draft considers resource providers and service recipients to be the primary users of service performance reports. Our own New Zealand study suggests that charities' resource providers, especially government and philanthropic funders, have their own information needs and use various accountability mechanisms to enforce and encourage the provision of both required and needed information. As such, resource providers may not rely on service performance reports to make their funding decisions.</p> <p>I am pleased to find that the representatives of service recipients are included in the primary user group. The current understanding of service recipients' own information needs is unfortunately still limited. While the information needs of service recipients (and their representatives) are sometimes assumed to be similar with resource providers, the information needs for these two groups of users may be largely different.</p> <p>The users who have limited powers of interrogation and rely on the service performance information for their accountability and decision making are likely to be individual donors (rather than large funders), volunteers, and general public. Thus, the users who rely on the service performance reports may be narrowly categorised.</p>	<p>Noted.</p> <p>Concur that larger resource providers may use both SPFR and GPFR.</p> <p>The research paper referred to by R7 has been included as agenda item 6.8 (supporting papers).</p>

R#	Comment	Staff response
	Further research is needed to understand the information needs and the extent to which key users, particularly service recipients and their representatives, utilise service performance reports for accountability and decision making.	
R7	<i>Dimensions of Performance</i> Agree [with no longer using the dimensions in the 2016 ED]	Noted
R7	<i>Reporting on Outputs and Reporting on Outcomes and Impacts</i> Agree [with deletion of these subsections in the 2016 ED]	Noted
	<b>Scope</b> Agree [with changes made to 2016 ED]	Noted
R7	<b>Definitions</b> Agree [with changes made to 2016 ED]	Noted
R7	<b>Principles</b> Agree with all changes in these sections, especially the emphasis of the neutrality in terms of “unfavourable” aspects of the entity’s service performance.  Our own research identifies that funders perceive an information need for <i>unintended outcomes</i> . The unintended outcomes are not necessarily unfavourable. They refer to achieved outcomes that differ from what the entity intends to achieve in the reporting periods. The reporting of unintended outcomes is recognised as an important type of information to tell a charity’s accountability story.  It may be useful to acknowledge the difficulty to achieve QCs <i>comparability</i> and <i>verifiability</i> in the context of qualitative measures and descriptions.	Noted  See Issue 1 <i>Subcommittee issues (QCs and disclosures)</i> and the suggested changes to discussion of verifiability in agenda items 2.9 and 6.5.
R7	<b>Information to be Reported</b> This section contains some significant changes compared to the 2016 Exposure Draft. The following comments are provided to further improve this section: <ul style="list-style-type: none"><li>Para.19 - an important factor <i>To whom the entity is accountable</i> may be considered. The accountability to resource providers, service recipients and organisational mission (with an internal focus) can be discharged by different accountability</li></ul>	



R#	Comment	Staff response
	<p>mechanisms. As such, it is important to consider the ‘to whom’ question and provide a balanced view of an entity’s performance for the reporting period. This factor may be the first question to consider in deciding what to report.</p> <ul style="list-style-type: none"> <li>Para. 19 (a) second example – it is difficult to picture a Not-for-profit entity that is merely responsible for the delivery of specific types and/or volume of goods or services to a target population, without attempting to make improvements on the conditions and status of the target population. In the example of an entity provides support services to elderly people in a city, it is reasonable to believe that the entity would consider beyond merely the delivery of support services. This example provides confusion to guide Tiers 1 and 2 not-for-profit organisations in analysing <i>what they are accountable/responsible for</i>.</li> <li>Para. 19 (c) – the explanatory notes may not entirely relevant to the factor how it went about achieving its service performance objectives. The focus of this section is suggested to be on whether planned service performance activities are delivered, and the extent to which the actual activities align with the planned activities i.e. what the entity intends to achieve. Then provide examples for both public sector and not-for-profit PBEs.</li> </ul>	<p>No change recommended. It is up to each entity to determine the balance of information provided in a general purpose financial report.</p> <p>No change recommended. The standard has been written for application by a range of entities. Although all entities might have a desire to improve the conditions and status of a target population this does not automatically mean that they are accountable for those changes, nor that they should report on them.</p> <p>Staff can see the point being made, but the intention of paragraph 19(c) is to cover the various ways that an entity might work with others. The points in paragraph 19 are prompts for information rather than specific requirements.</p>
R7	<p><b>Performance Indicators</b></p> <p>Agree. The information on internal activities is essential for the entities that value their organisational mission (why it exists) more than some other factors. The reporting of this information will also help the users to assess the overall performance of PBEs.</p>	Noted
R7	<p><b>Presentation</b></p> <p>While understanding the Board follows a high-level principles-based approach in this revised proposal, different templates adopted by Tiers 1 and 2 charities may impede users to compare relevant service performance information that is available with Charities Register.</p>	The reasons for adopting a principles based approach are outlined in the feedback statement and the BC. Less comparability is a consequence of allowing flexibility.
R7	<p><b>Comparative Information and Consistency of Reporting</b></p> <p>Agree</p>	Noted

R#	Comment	Staff response
R7	<b>Disclosure of Judgements</b> Agree	Noted
R7	<b>Effective Date</b> Agree	Noted See Issue 5 <i>Effective date</i> in agenda item 6.2.
R7	<b>Amendments to other standards</b> Agree	Noted
R7	<b>Guidance</b> Agree. It is essential to develop sector-appropriate guidance and provide exemplars for both Tiers 1 and 2 not-for-profit organisations in order to avoid confusion in applying this revised proposal. [Information about RSM omitted]	See Issue 7 <i>Comments on guidance</i> in agenda item 6.2. The NZASB has decided to focus on guidance for smaller Tier 2 NFPs on the grounds that these entities are most likely to benefit from guidance.
R8	On behalf of both the Commerce Commission and the Electricity Authority, I can confirm that we have no further substantive comments on the XRB's draft Standard on Service Performance Reporting. We are pleased to note that much of our feedback was incorporated into this revised draft, particularly the removal of the requirement to report performance in terms of outputs, impacts and outcomes to make the Standard less prescriptive.	Support noted.
R9	The Institute of Directors (IoD) appreciates the opportunity to provide further comment on the introduction of a PBE Standard on service performance reporting by commenting on the Limited Scope Review Draft. The new Standard will apply to Tier 1 and Tier 2 public benefit entities (PBEs), both public and not-for-profit entities.  In the IoD submission (July 2016) on the Exposure Draft of the Standard (ED NZASB 2016–6) we noted our support for the introduction of a standard to provide PBEs with a framework for service performance reporting. Financial information alone doesn't tell the whole story and accurate, timely and meaningful non-financial information is essential for	

R#	Comment	Staff response
	<p>good governance. It helps enable the board to monitor performance, hold management to account and make more effective decisions.</p> <p>We note that the NZASB is seeking comment specifically on the workability of the revised Standard and if there may be any unintended consequences. We re-iterate the comments made in our earlier submission and comment specifically on the changes in the revised Standard below.</p> <p>[Information about IOD omitted]</p>	
R9	<p><b>Comments on revised Standard proposals</b></p> <p>We support the changes in the revised Standard, including a more flexible approach to what service performance information is reported and the extended period before implementation of the new Standard. We expect these changes will assist the workability of a new service performance reporting regime.</p>	Support noted.
R9	<p><b>Information to be reported</b></p> <p>The revised Standard changes the requirements on what service performance information should be reported. The dimensions described as outputs, outcomes and impacts in the Exposure Draft have been replaced with higher level principles describing the information to be reported in more general terms. The revised Standard requires entities to provide users with:</p> <ul style="list-style-type: none"> <li>a) Sufficient contextual information to understand why the entity exists, what it intends to achieve in broad terms over the medium to long term, and how it goes about this; and</li> <li>b) Information about what the entity has done during the reporting period in working towards its broader aims and objectives, as described in (a).</li> </ul> <p>We support this approach as providing more flexibility for entities. It is important that the framework is not too prescriptive and enables the provision of useful and relevant information for management and governance purposes. It is also important that it doesn't become overly compliance focused and that there is an appropriate balance between accountability for annual performance and working towards longer term objectives.</p>	Support for flexibility noted.

R#	Comment	Staff response
R9	<p><b>Disclosure of judgements</b></p> <p>The revised Standard includes a new requirement that entities disclose the critical judgements it made that are relevant to understanding the entity's service performance information (such as in relation to the selection and aggregation of information).</p> <p>We note that this is a consequence of the less prescriptive approach to the information to be reported and agree that it is a necessary counterbalance for a more flexible framework for reporting information. However it is also critical that the information reported is meaningful to the entity, and as stated in the Standard (21(b)) is 'not so much information that it could obscure the overall picture'.</p>	Support noted.
R9	<p><b>Effective date for implementation</b></p> <p>Introducing the new service performance reporting regime will mean significant change for many PBEs, particularly in the not-for-profit sector where this will be a new requirement.</p> <p>Financial reporting is underpinned by professional qualifications and training, but there isn't such well-established capability in respect of non-financial reporting.</p> <p>In our submission on the Exposure Draft we advocated for a phased approach (e.g. over 3 to 5 years) for implementing the new standard. We considered the proposed two-year implementation period was insufficient to enable effective transition to a new performance reporting regime for many PBEs.</p> <p>We are pleased to see the extended period before the new standard will be applied, for annual reporting periods on or after 1 January 2021 (with early adoption permitted). We consider this longer transition period will better support awareness raising and capability building in PBEs, and the accounting and auditing professions, for the new performance reporting regime.</p> <p>The extended period will also provide boards and others charged with responsibility for governance more time to deepen their understanding of the new reporting regime to enable them to fulfil their responsibilities effectively.</p>	<p>Support for proposed effective date noted.</p> <p>See Issue 5 <i>Effective date</i> in agenda item 6.2.</p>

R#	Comment	Staff response
R9	<p><b>Conclusion</b></p> <p>Performance reporting on financial and non-financial information is important for effective decision- making and accountability purposes.</p> <p>The introduction of service reporting requirements will mean significant change for many PBEs. We support the proposed flexibility in how entities report service performance information and the extended implementation period. We also encourage the development of clear guidance and educational support for PBE entities.</p> <p>The IoD appreciates the opportunity to make a submission on behalf of its members and we would be happy to discuss this submission.</p>	Noted
R10	<p>We are pleased to comment on the revised proposals outlined in the Limited Scope Review Draft of PBE FRS XX <i>Service Performance Reporting</i> (“revised ED”). As mentioned in our comment letter on the original <i>Exposure Draft NZASB 2016-6: Service Performance Reporting</i> (“original ED”), we are supportive of the NZASB’s project to establish a specific standard for reporting service performance. The final standard will provide Public Benefit Entities (PBEs) with a framework for reporting non-financial information, aligning reporting with their primary objective to provide goods or services for a community or social benefit. We believe the proposals will improve PBEs’ accountability to users of financial statements, as well as enhancing decision making within an organisation.</p> <p>Our key concern with the original ED related to the application of its requirements to not-for-profit PBEs (particularly smaller ones in Tier 2) and ensuring there is an appropriate balance between cost of implementation and the benefits. Specifically, we were concerned that smaller PBEs may find it difficult and costly to comply with the original ED’s requirements around the disclosure of the impacts that the entity has had on its outcomes. We note that the revised ED no longer requires the disclosure of outputs, outcomes or impacts. This applies to both Tier 1 and Tier 2 PBEs. We also note generally that the revised ED is less prescriptive than the original ED and provides PBEs with greater flexibility around reporting on their service performance. Therefore we believe that our abovementioned key concern is addressed by the revised ED.</p>	Note support for changes

R#	Comment	Staff response
	<p>In our view, the key risk regarding the revised ED is that the degree of flexibility provided by the less prescriptive and more high-level nature of its requirements may potentially be too high. As such, PBEs' interpretation of the proposed new standard may result in some useful service performance information not being reported. Generally, we believe that the revised ED's requirement to disclose critical judgements should mitigate this risk to some extent. However, we believe it would be useful to include additional requirements or guidance around reporting on the longer-term effects of a PBE's activities on society or a social group (i.e. reporting against what the original ED referred to as "outcomes"), where it is appropriate for an entity to report on this aspect of service performance. Having said this, we understand the challenge around including such requirements/ guidance in a standard that applies to a wide range of PBEs.</p> <p>We also note that the less prescriptive and more high-level nature of the requirements in the revised ED may result in a lower level of comparability across different entities as compared to the original ED. However, we believe that this is mitigated to some extent by the requirement in the revised ED to disclose critical judgements made in reporting service performance, as well as the requirement to comply with the qualitative characteristics, including comparability.</p> <p>Other than the matters described above, we do not have significant concerns around the workability of the revised ED or any potential unintended consequences arising from the revised ED.</p> <p>For a more detailed response, please refer to the attached appendix.</p> <p>Please do not hesitate to contact us should you have any queries. We also would be happy to meet with you to discuss our comments further.</p>	See Issue 7 <i>Comments on guidance</i> in agenda item 6.2.
R10	<p><b>Appendix A – Response to specific Limited Scope Review question</b></p> <p><u>Key changes in the revised ED:</u></p> <p>We note that the key changes in the revised ED as compared to the original ED are:</p>	

R#	Comment	Staff response
	<p>(1) The requirements of the revised ED are less prescriptive and more high-level than the original ED. For example, unlike the original ED, the revised ED no longer refers to, or requires disclosure of, outputs, outcomes or impacts. Instead, the revised ED requires entities to provide: (a) sufficient contextual information to understand why the entity exists, what it intends to achieve in broad terms over the medium to long term, and how it goes about this, and (b) information about what the entity has done during the reporting period in working towards its broader aims and objectives.</p> <p>(2) The revised ED requires entities to disclose critical judgements made when reporting service performance information, i.e. those judgements that have the most significant effect on the selection and aggregation of service performance information, and that are relevant to an understanding of the entity's service performance information.</p>	
R10	<p><u>Workability and potential consequences of the revised ED as a result of the above key changes:</u></p> <p><i>(a) Advantages of revised ED</i></p> <p>We believe that the above changes have several advantages in terms of enhancing the workability of the revised ED. For example, the key concern that we had with the original ED related to the application of its requirements to not-for-profit entities, particularly smaller ones in Tier 2, and ensuring there is an appropriate balance between cost of implementation and the benefits. Specifically, we were concerned that smaller entities may find it difficult and costly to comply with the original ED's requirements of having to establish whether there is clear evidence of a link between the entity's outputs and the actual impact on outcomes, and if such evidence existed, to report on the entity's impacts on outcomes. We therefore suggested that Tier 2 PBEs be exempt from the requirement around impacts. As noted above, the revised ED has altogether removed the requirement to report on impacts, as well as outputs and outcomes, for both Tier 1 and Tier 2 PBEs. In addition, although the revised ED has not introduced Tier 2 disclosure concessions, as noted above it is generally much less prescriptive than the original ED. Therefore the proposals in the revised ED should be easier and less costly to apply for all PBEs, including not-for-profit PBEs in Tier 2.</p>	Support for critical judgements noted.

R#	Comment	Staff response
	<p>In addition, the move towards more general service performance reporting requirements gives PBEs greater freedom and flexibility to “tell their story” in a way that is tailored – and therefore most relevant and meaningful – to the specific PBE and its users. At the same time, the revised ED still specifically requires PBEs to provide disclosures on what they intend to achieve in the longer term and what they have provided during the year in terms of service performance, thereby still aligning PBEs’ reporting requirements with their primary objective to provide goods or services for a community or social benefit.</p> <p>We also note that the more general requirements of the revised ED will help avoid potential inconsistencies between the proposed standard and the terminology and requirements contained within the various pieces of legislation that require public sector PBEs to report on their service performance.</p> <p>In terms of the requirement to disclose critical judgements, we believe that it will enhance the transparency of PBEs’ service performance reports. Furthermore, we agree with the NZASB’s comment in the Basis of Conclusion of the revised ED that the requirement to disclose critical judgement is a “necessary counterbalance” to the less prescriptive requirements of the revised ED. Specifically, we believe that the requirement to disclose critical judgements will to some extent mitigate certain concerns that arise from the move to more high-level requirements, as explained below.</p>	
R10	<p><i>(b) Discussion of potential risks arising from the revised ED</i></p> <p>While we acknowledge the benefit of flexibility around service performance reporting requirements, we believe that there is a risk that the degree of flexibility provided by the less prescriptive and more high-level nature of the requirements in the revised ED may potentially be too high. As such, there is a potential risk that some useful service performance information, which would have been required under the original ED, may not be disclosed by PBEs under the revised ED. In general, the revised ED provides requirements that mitigates these risks. For example, we note that the original ED included an explicit requirement to explain the link between a PBE’s outputs and expected outcomes. Such an explanation arguably enhances the understandability and therefore usefulness of service performance information, as without it there is a risk that PBEs will report on their service performance by disclosing their wider service performance</p>	<p>Noted.</p> <p>Respondent discusses the risks associated with increased flexibility (compared to the 2016 ED) and how these risks have been mitigated, to some extent, by disclosures about critical judgements.</p> <p>Respondent refers to the approach in the 2016 ED as a viable option. However, some respondents to the 2016 ED strongly disagreed with requirements based on outputs and</p>



R#	Comment	Staff response
	<p>objectives and providing a list of goods/service produced during the year, but there may be a “disconnect” between the two elements. We note that the requirement to explain the link between outputs and expected outcomes was removed in the revised ED. However, we believe that this is mitigated by the revised ED’s requirement to disclose critical judgements, as paragraph 46(a) of the revised ED requires PBEs to consider “<i>the extent to which the entity’s service performance information is consistent with and clearly linked to the entity’s overall purpose and strategies</i>”, and states that “[i]f it is not, users may need to understand why not”. Thus the revised ED still ensures that it is clear to users how the goods, services or other aspects of service performance reported on by a PBE are connected to the PBE’s wider service performance goals.</p> <p>However, in other cases, while the risk around useful information not being disclosed is mitigated to a certain extent, we believe that more detailed requirements or additional guidance could be beneficial. For example, it could be argued that the requirements in the original ED to report on outputs, outcomes and impacts, and to disclose performance measures with regards to outputs and impacts on outcomes, will have helped ensure a certain minimum level of information and structure in service performance reports, which would have been useful for users. These requirements arguably would have been useful to the reporting entity, in terms of providing a degree of clarity as to what it is expected to include in its service performance report. While the revised ED no longer requires PBEs to report on outputs, outcomes or impacts, it still specifically requires PBEs to provide contextual information on their broad service performance objectives and methods (which needs to draw on the entity’s performance framework, theory of change or intervention logic, if used, and explain the main ways in which the PBE carries out service performance activities (paragraph 17-18)), and to report what they have provided during the year in terms of service performance (by providing an appropriate mix of service performance measures and/or descriptions). Further, the revised ED includes some guidance around performance measures, such as general examples of performance measures and descriptions (paragraph 20) and specific examples of possible performance measures and descriptions for reporting on goods and services provided (paragraphs 27-28). Therefore, while less prescriptive and more flexible, the revised ED still contains certain specific requirements and guidance around information to be disclosed. In</p>	<p>outcomes or indicated differing uses of terminology.</p> <p>See Issue 7 <i>Comments on guidance</i> in agenda item 6.2.</p>

R#	Comment	Staff response
	<p>addition, the requirement in the revised ED to disclose critical judgements should ensure that the reason for including or excluding certain service performance information is clear to users, and the overarching requirement to provide service performance information that is appropriate and meaningful for users, should help ensure that the service performance information provided to users is sufficient and useful.</p> <p>However, it is possible that PBEs may need additional guidance when applying these less prescriptive requirements. We believe that this applies particularly to PBEs that report on the longer-term effects of their activities on society (similarly to what the original ED referred to as “outcomes”). We do not expect all PBEs within the scope of the proposed standard to be required to report on their performance against such social outcomes. For example, as noted in paragraph 19(a) of the proposed ED, a not-for-profit PBE that is responsible for providing certain goods or services to a group in the community, it would be appropriate to focus on goods or services produced during the year in its service performance report. However, for certain PBEs, especially in the public sector, reporting on longer-term social effects would provide useful information for users and help discharge the entity’s accountability. We note that some guidance exists in the revised ED regarding reporting on performance against longer-term social effects of a PBE’s activities (for example, paragraph 25 says that performance measures “may be used to inform assessments of the broad or longer-term effects of a project or an entity’s work” on recipients of goods/services or a group of society – such as changes in educational achievements or poverty levels). However, generally, the revised ED seems to have a greater focus, or at least more guidance, on reporting on what has been produced during the year. Therefore, while we do not argue that the proposed standard should require all PBEs in Tier 1 and 2 to report on the long-term effect of their activities on society, we believe that additional requirements or guidance in this area would be useful. Such guidance will give PBEs that report on the longer-term social effects of their activities greater clarity as to how they are expected to report on this, and will help ensure that useful information is provided to users. Having said this, we understand the challenge around including such requirements/guidance, given that the proposed standard will apply to a wide range of different PBEs, i.e. both Tier 1 and Tier 2 PBEs across both the public and not-for-profit sectors.</p>	

R#	Comment	Staff response
	<p>Another potential concern with the less prescriptive approach of the revised ED is a possible lack of comparability in service performance reports across different PBEs. In our comment letter on the original ED, we noted that the proposals as originally drafted will improve consistency in service performance reporting between entities with similar activities and between reporting periods. Given the less prescriptive and more high-level nature of the requirements in the revised ED, it is possible that service performance reporting may be less consistent across entities as compared to the consistency that will have been achieved by the original ED. This applies especially to PBEs in the not-for-profit sector, where – unlike in the public sector – there is no legislation that requires service performance reporting. However, we believe that the requirement in the revised ED to disclose critical judgements will help mitigate this concern to some extent. For example, paragraph 44 of the revised ED acknowledges that entities need to apply judgement when deciding on an appropriate and meaningful mix of performance measures (as per paragraphs 21-22), and requires entities to disclose the critical judgements applied in this regard. In addition, the revised ED still requires service performance information to comply with the qualitative characteristics, including comparability.</p> <p>Finally, it could be argued that the benefits of the more prescriptive requirements in the original ED may have outweighed the cost of complying with these requirements for Tier 1 PBEs, therefore there would have been merit in retaining the more prescriptive requirements of the original ED and providing Tier 2 disclosure concessions. However, it is not clear that the merits of such an approach would be greater than the abovementioned benefits of the NZASB's chosen approach, namely the benefits of greater flexibility, more tailored information and lower compliance costs to both Tier 1 and Tier 2 PBEs, as well as lack of conflict with legislative requirements for public sector PBEs. In addition, as noted above, the requirements in the revised ED to disclose critical judgements, comply with the qualitative characteristic of comparability and provide information that is appropriate and meaningful to users should help mitigate the potential concern around comparability and ensure that PBEs provide service performance information that is useful to users. However, please note the abovementioned discussion around the potential risk</p>	

R#	Comment	Staff response
	associated with a high degree of flexibility in the revised ED, which could be mitigated by additional guidance.	
R10	<p><u>Other comments on the revised ED:</u></p> <p>Additionally, we note the following with regards to the revised ED:</p> <ul style="list-style-type: none"> <li>- The revised ED has added an emphasis on neutrality when requiring service performance information to be faithfully representative. We believe that this will help ensure that both good and poor service performance is reported, which will enhance PBEs' accountability and the usefulness of service performance information for users.</li> <li>- The revised ED increases the implementation period of the proposed requirements from 2 years to 3 years. We believe that this enhances the workability of the proposed standard, as it will allow PBEs, particularly not-for-profit PBEs, sufficient time to update their systems and processes and ensure that the new standard is properly implemented.</li> <li>- We note that under the standards <i>PBE Simple Format Reporting – Accrual</i>, Tier 3 public sector PBEs whose legislation requires service performance reporting and all Tier 3 not-for profit PBEs are required to report on their outputs and outcomes in a statement of service performance. By contrast the revised ED, which will apply to Tier 1 and Tier 2 PBEs, does not specifically refer to outputs and outcomes. We suggest that the NZASB considers whether <i>PBE Simple Format Reporting – Accrual</i> should be amended in this respect to be consistent with the revised ED.</li> </ul>	<p>Note support for increased emphasis on neutrality</p> <p>Note support for proposed effective date See issue 5 <i>Effective date</i> in agenda item 6.2.</p> <p>See Issue 9 <i>Difference between Tiers</i> in agenda item 6.2.</p> <p>The NZASB's Strategic Action Plan includes <i>Action 1C.2: Post-implementation Review of Tier 3 and Tier 4 PBE Accounting Requirements</i>.</p>
R11	<p>We read the revised draft PBE FRS, <i>Service Performance Reporting</i> standard and the feedback statement on ED NZASB 2016-6.</p> <p>We appreciate that you have taken into careful consideration the comments received from the respondents. We believe that the current draft of the standard has achieved the purpose of being a high-level guidance to the public benefit entities especially those that have existing legislative requirements.</p> <p>We also support that comparatives should be included, as relevant, to promote consistency of the service performance reports and the disclosure of significant judgements.</p> <p>With the above, we don't have further comments on the revised draft.</p>	Support noted.

## SERVICE PERFORMANCE REPORTING



NZ ACCOUNTING  
STANDARDS  
BOARD

## Service Performance Reporting

### Issued [month/year]

This Standard was issued on [Date] by the New Zealand Accounting Standards Board of the External Reporting Board pursuant to section 12(a) of the Financial Reporting Act 2013.

This Standard is a disallowable instrument for the purposes of the Legislation Act 2012, and pursuant to section 27(1) of the Financial Reporting Act 2013 takes effect on [Date].

Reporting entities that are subject to this Standard are required to apply it in accordance with the effective date, which is set out in paragraph 47.

In finalising this Standard, the New Zealand Accounting Standards Board has carried out appropriate consultation in accordance with section 22(1) of the Financial Reporting Act 2013.

This Standard has been issued to establish requirements for service performance reporting by Tier 1 and Tier 2 public benefit entities.

## SERVICE PERFORMANCE REPORTING

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## SERVICE PERFORMANCE REPORTING

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Public Benefit Entity Financial Reporting Standard XX *Service Performance Reporting* is set out in paragraphs 1–47 and Appendix A. All the paragraphs have equal authority. PBE FRS XX should be read in the context of its objective, the NZASB’s Basis for Conclusions on PBE FRS XX, the *Public Benefit Entities’ Conceptual Framework* and Standard XRB A1 *Application of the Accounting Standards Framework*. PBE IPSAS 3 *Accounting Policies, Changes in Accounting Estimates and Errors* provides a basis for selecting and applying accounting policies in the absence of explicit guidance.

## SERVICE PERFORMANCE REPORTING

**Introduction****Reasons for Issuing the Standard**

- IN1 The New Zealand Accounting Standards Board (NZASB) has issued this Standard to establish requirements for the reporting of service performance information in order to better meet the needs of users of general purpose financial reports of public benefit entities. Public benefit entities have aims and objectives that relate to serving the community or society (or a section thereof). They seek to achieve these aims and objectives by using funds received from resource providers (for example, taxpayers, ratepayers, donors and grantors) to undertake activities for community or social benefit. Therefore, service performance information is an important part of their general purpose financial reports.
- IN2 Service performance information is information about what the entity has done during the reporting period in working towards its broader aims and objectives, together with supporting contextual information.
- IN3 This Standard establishes high-level requirements because:
- (a) Service performance reporting is an area of reporting that continues to evolve;
  - (b) Entities may be subject to a range of service performance reporting requirements, including legislative requirements and may use a variety of performance frameworks; and
  - (c) It provides flexibility for entities to determine how best to 'tell their story' in an appropriate and meaningful way.

**Accountability and Decision Making**

- IN4 The primary users of general purpose financial reports of public benefit entities are resource providers (for example, taxpayers, ratepayers, donors, grantors and lenders) and service recipients, and their representatives. Users of general purpose financial reports of public benefit entities rely on those reports for information that is useful for accountability and decision making. Financial statements provide some, but not all, of the information users require.
- IN5 Although the exact nature of users' interests in an entity's service performance information will be influenced by a number of factors (for example, the nature of an entity's functions, the extent to which it can influence society or segments of society, and the nature of its agreements with funders and other entities) they generally have some common interests. They are generally interested in whether an entity has used funds for the purpose intended, what it has achieved with the resources available to it, and whether it could have done more with those resources. They may also be interested in forming judgements about what an entity could do with additional resources.

**Main Features of the Standard**

- IN6 This Standard establishes requirements for the selection and presentation of service performance information. It requires<sup>1</sup> that an entity:
- (a) Present its service performance information and financial statements in the same general purpose financial report;
  - (b) Apply the qualitative characteristics of information and the pervasive constraints on information identified in the *Public Benefit Entities' Conceptual Framework* (PBE Conceptual Framework). It states that application of the qualitative characteristics and appropriate balancing of the constraints on information results in service performance information that is appropriate and meaningful to the users of general purpose financial reports;
  - (c) Except as otherwise required by legislation, present service performance information for the same reporting entity and reporting period as the financial statements;
  - (d) Provide users with (i) sufficient contextual information to understand why the entity exists, what it intends to achieve in broad terms over the medium to long term, and how it goes about this; and (ii) provide users with information about what the entity has done during the reporting period in working towards its broader aims and objectives;

<sup>1</sup> [As explained in the Standard, there are some exceptions to these requirements. \[Footnote prompted by comment from R12\]](#)



For consideration at the NZASB September 2017 meeting.

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- (e) Disclose critical judgements made in reporting service performance information that are relevant to an understanding of the entity's service performance information;
- (f) Clearly identify the service performance information presented in accordance with the Standard; and
- (g) Provide comparative information.

IN7 These requirements draw upon the concepts in the PBE Conceptual Framework including the objective of general purpose financial reporting, the users of general purpose financial reports and their information needs, and the qualitative characteristics.

SERVICE PERFORMANCE REPORTING

## Objective

1. **The objective of this Standard is to establish principles and requirements for an entity to present service performance information that is useful for accountability and decision-making purposes in a general purpose financial report.**
2. Service performance information is information about what the entity has done during the reporting period in working towards its broader aims and objectives, together with supporting contextual information.

## Scope

3. **This Standard applies to:**
  - (a) **All Tier 1 and Tier 2 not-for-profit public benefit entities; and**
  - (b) **Tier 1 and Tier 2 public sector public benefit entities required by legislation to provide information in respect of service performance in accordance with generally accepted accounting practice (GAAP). If an entity is required by legislation to report service performance information on only some of its activities, this Standard applies only to those activities.**
4. This Standard does not apply to service performance information that is condensed, prospective or summarised. PBE IAS 34 *Interim Financial Reporting*, PBE FRS 42 *Prospective Financial Statements*, and PBE FRS 43 *Summary Financial Statements* establish requirements for service performance information presented in general purpose reports that include interim financial statements, prospective financial statements and summary financial statements respectively. This Standard does not apply to other non-financial information presented in a general purpose financial report (for example, information about an entity's performance relating to its environmental goals or values), unless this information is directly linked to its service performance.
5. Nonetheless application of the principles and requirements of this Standard to service performance information outside the scope of this Standard is encouraged to the extent applicable.

## Principles

6. **An entity shall present service performance information that is useful for accountability and decision-making purposes in the same general purpose financial report as its financial statements. Presentation of service performance information together with financial statements enables users to make assessments of the entity's performance.**
7. **In selecting and presenting service performance information in a general purpose financial report an entity shall apply the qualitative characteristics of information and the pervasive constraints on information identified in the *Public Benefit Entities' Conceptual Framework* (PBE Conceptual Framework). Application of the qualitative characteristics and appropriate balancing of the constraints on information results in service performance information that is appropriate and meaningful to the users of general purpose financial reports.**
8. The qualitative characteristics of information included in general purpose financial reports are the attributes that make that information useful to users and support the achievement of the objectives of financial reporting. The qualitative characteristics identified in the PBE Conceptual Framework are relevance, faithful representation, understandability, timeliness, comparability, and verifiability. Each of the qualitative characteristics is integral to, and works with, the other characteristics to provide information useful for achieving the objectives of financial reporting in general purpose financial reports. However, in practice, all qualitative characteristics may not be fully achieved, and a balance or trade-off between certain of them may be necessary. An entity considers the needs of users and the objectives of financial reporting in the application of the qualitative characteristics to service performance information.
9. When applying the qualitative characteristics to service performance information the following are important:
  - (a) **Relevance:** Relevance is particularly important in selecting and aggregating service performance information. Relevance is strongly linked with judgements about the materiality of information

## SERVICE PERFORMANCE REPORTING

and the appropriate level of aggregation of information. Relevant information assists users in forming assessments about an entity's accountability for service performance and in making decisions that rely on information about service performance (for example, whether to provide funding to an entity or whether to work with an entity in the pursuit of common goals). Relevance should be applied in considering what, and how much, to report on service performance. Relevance and understandability should be considered together because both the amount of information and the level of detail presented can affect understandability.

- (b) Faithful Representation: To be useful, service performance information must be a faithful representation of the entity's service performance. Faithful representation is attained when the service performance information is complete, neutral, and free from material error. Completeness implies that the service performance information presents an overall impression of the entity's service performance with appropriate links to financial information. Neutrality is the absence of bias. For service performance information to be neutral it needs to report on both favourable and unfavourable aspects of the entity's service performance in an unbiased manner. [Free from material error means that there are no errors or omissions that are individually or collectively material in the service performance information. \[Suggestions for consideration by NZASB and NZAuASB subcommittee members at meeting on 5 September 2017\]](#)
  - (c) Understandability: Service performance information should be communicated to users simply and clearly. The amount of information presented affects understandability.
  - (d) Timeliness: Service performance information should be reported to users before it loses its capacity to be useful for accountability and decision-making purposes.
  - (e) Comparability: Service performance information should provide users with a basis and context to compare an entity's service performance over time, and where appropriate, against planned performance or the performance of other entities.
  - (f) Verifiability: [This is the quality of information that helps assure users that service performance information faithfully represents the entity's service performance. To be verifiable, service performance information needs to be capable of measurement or description in a consistent manner, be capable of independent verification and exclude unsubstantiated claims. When Service performance information is verifiable when the assumptions underlying the information are explicit, the methodologies adopted in compiling that information and the factors and circumstances that support any opinions expressed or disclosures made are transparent. This enables users are able to form judgements about the appropriateness of those assumptions and the method of compilation, measurement, representation and interpretation of the information. \[Suggestions for consideration by NZASB and NZAuASB subcommittee members at meeting on 5 September 2017\].](#)
10. The pervasive constraints on information identified in the PBE Conceptual Framework are materiality, cost-benefit and balance between the qualitative characteristics. All of these constraints are important for selecting information in service performance reports and the level of detail that is provided.

## Information to be Reported

### Reporting Entity and Reporting Period

- 11. **Except as otherwise required by legislation, an entity shall present service performance information for the same reporting entity and reporting period as the financial statements.**
- 12. The reporting entity and reporting period concepts are relevant for both financial statements and service performance reporting. This Standard discusses some additional factors that need to be considered when applying these concepts to service performance information.
- 13. If the reporting entity is an economic entity comprising a controlling entity and controlled entities then service performance is reported in respect of that entire economic entity. If the reporting entity is a single entity, then service performance is reported in respect of that single entity. Where legislation or regulation requires service performance information to be prepared for a reporting entity that differs from the reporting entity for which historical general purpose financial statements are presented, an entity is compelled to comply with such legislation or regulation.

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14. This Standard establishes requirements for reporting on an entity's service performance for a reporting period. However, public benefit entities often have long-term service performance objectives. Judgement is required in deciding how much information to provide about the entity's service performance in the current reporting period and how much information to provide about progress towards its long-term objectives. In reporting on its current period's service performance an entity is likely to need to provide information that relates to previous periods or future periods (such as trend data) to provide context.

**Service Performance Information**

15. **An entity's service performance information shall:**
- (a) **Provide users with sufficient contextual information to understand why the entity exists, what it intends to achieve in broad terms over the medium to long term, and how it goes about this; and**
  - (b) **Provide users with information about what the entity has done during the reporting period in working towards its broader aims and objectives, as described in (a) above.**
16. Paragraph 15 establishes requirements about the service performance information to be reported. Presentation of service performance information is discussed in paragraphs 29 to 35.
17. Paragraph 15(a) requires contextual information about why an entity exists, what it intends to achieve and how it goes about this. This information should be drawn from relevant documents such as founding documents, governance documents, accountability documents and planning documents. For example, a not-for-profit entity would consider documents such as its constitution, trust deed, mission statement (vision, purpose) and its most recent plans and strategies. If an entity uses a performance framework, theory of change or intervention logic at its highest level of management or in the governance of the entity, the contextual information should also draw upon that performance framework, theory of change or intervention logic. For example, a local authority's Long-Term Plan provides a meaningful performance framework for its activities.
18. In providing the contextual information required by paragraph 15(a), an entity shall explain the main ways in which it carries out its service performance activities. For example:
- (a) Delivering goods and services directly to individuals, entities or groups (including members);
  - (b) Working together with other entities that share common objectives;
  - (c) Contracting with other entities to deliver goods and services on their behalf; or
  - (d) Making grants to other individuals or entities.
19. The nature of the information that an entity provides to meet the requirements of paragraph 15(b) will depend on the circumstances of the entity. An entity shall consider all of the following factors in deciding what to report.
- (a) *What it is accountable/responsible for.* Some entities have responsibility for working towards particular improvements in the health, education, welfare and/or social or economic well-being of individuals or a segment of society. For example, a public sector entity may be required to target its resources to reduce disparity in educational achievement between different groups in society. In this case, the entity's service performance information is likely to focus on whether and the extent to which those particular improvements occurred. In other cases, entities are primarily responsible for the delivery of specific types and/or volume of goods or services to a target population, rather than trying to bring about particular improvements in the health, education, welfare and/or social or economic well-being of the recipients of those goods and services. For example, an entity may be required to provide support services to elderly people in a city. In that case, the entity's service performance information is likely to focus on the delivery of the specified goods or services. Even in cases where an entity determines the nature and extent of its service performance itself, it will need to consider the nature of its accountability to funders and service recipients.
  - (b) *What it intended to achieve during the reporting period.* The information that an entity provides about its planned performance will be influenced by how much information the entity has previously published about its planned performance. If a not-for-profit entity has identified specific performance goals or targets when obtaining funding from other parties, its service

# SERVICE PERFORMANCE REPORTING

performance information is likely to focus on reporting whether, and/or the extent to which, it met those goals or targets. If a not-for-profit entity has been working towards general service performance objectives for the reporting period (for example, a planned increase in the range or volume of goods or services provided or a planned improvement in the entity's effect on a target population) rather than specific service performance goals or targets, its service performance information is likely to focus on reporting whether, and/or the extent to which, it made progress in relation to those general objectives. Public sector entities are often required to publish information about planned performance in planning documents. In such cases this Standard requires comparisons between actual and planned performance (see paragraph 37).

- (c) *How it went about achieving its service performance objectives.* If an entity delivers goods and services in conjunction with another entity or collaborates with another entity in seeking to achieve its service performance objectives and goals, it needs to consider the most appropriate and meaningful way of reporting on its service performance. If an entity has agreed to deliver goods and services and then contracts with another entity to deliver those goods and services on its behalf, the first entity generally remains accountable for reporting on the delivery of those goods and services. If an entity makes grants to other entities to be used by those entities in delivering goods and services, the entity needs to exercise judgement in deciding whether to report solely on its funding activities or to include information about the goods and services provided by those other entities. In the public sector a department may administer an appropriation used by another department or it may use an appropriation administered by another department. The information a department includes in its service performance information will reflect which department has responsibility for reporting on such appropriations.
- (d) *Other factors* relevant to an understanding of its service performance during the period, such as the links between its financial statements and service performance information and/or external social, legal or economic factors (for example, changes in funding levels that affect its service performance).

## Performance Measures and/or Descriptions

20. **In reporting on what an entity has done during the reporting period an entity shall provide users with an appropriate and meaningful mix of performance measures and/or descriptions for the reporting period. The performance measures and/or descriptions used by an entity to communicate its service performance may be:**
  - (a) **Quantitative measures:** Examples of quantitative measures are the quantity of goods and services, the cost of goods and services, the time taken to provide goods and services, levels of satisfaction using a rating scale on a questionnaire or survey, and numerical measures for service performance objectives or goals;
  - (b) **Qualitative measures:** Examples of qualitative measures are descriptors such as compliance or non-compliance with a quality standard, ratings such as high, medium or low, or ratings assigned by experts; or
  - (c) **Qualitative descriptions:** Examples of qualitative descriptions are those based on participant observations, open-ended questions on interviews and surveys and case studies. For example, **how did an entity's service performance activities change the well-being and circumstances of a client group?** [\[Text bolded following comments by R5 and R6.\]](#)
21. An entity shall exercise judgement to select an appropriate and meaningful mix of performance measures and/or descriptions so as to provide users of its financial [reportstatements](#) with sufficient, but not excessive, information about its service performance for the period. In determining the type and extent of information to provide, the entity considers a balance between providing: [\[edit following comments from R6\]](#)
  - (a) Enough information to provide users with an overall picture of its service performance for the period; and
  - (b) Not so much information that it could obscure the overall picture.
22. In selecting the performance measures and/or descriptions to be reported an entity shall consider the qualitative characteristics and the constraints on information in general purpose financial reports.

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Judgement is needed to determine the most appropriate and meaningful performance measures and/or descriptions to be reported. The most appropriate and meaningful performance measures and/or descriptions are those that measure or describe aspects of performance that are of particular value or importance for accountability or decision-making purposes. [staff edit]

23. In general, performance measures and/or descriptions shall have an external focus. However, this does not preclude an entity from providing information on internal activities, processes, plans or policies if it considers that this information provides important context for its service performance.
24. Performance measures and/or descriptions may be used to inform assessments of efficiency and effectiveness or they may attempt to provide information directly on an entity's efficiency and effectiveness in relation to its service performance.
25. Performance measures and/or descriptions may be used to inform assessments of the broad or longer-term effects of a project or an entity's work (also referred to as the difference the entity makes) on individuals who are direct recipients of a project or an entity's work, effects on those who are not direct recipients, or effects on society or subgroups of society. Examples of broad or longer-term effects include changes to these individuals' and groups' educational achievements or health, or changes to groups' or societal poverty and crime levels, or changes to the health of different groups within society. [Editorial suggestion from R2]
26. Performance measures and/or descriptions are more useful when they are accompanied by comparisons (for example, comparisons over time (trend data), comparisons by population or provider subgroups, international comparisons and comparisons against a target or standard).
27. If an entity determines that reporting on goods and services delivered provides appropriate and meaningful service performance information, performance measures and/or descriptions for goods and services may include:
  - (a) The quantity of the goods and services;
  - (b) The quality of the goods and services;
  - (c) The timeframe over which the goods and services were produced;
  - (d) The physical location where the goods and services were delivered; and
  - (e) The cost of the goods and services.
28. Reporting on the cost of goods and services provides an important link between the financial statements and service performance information. However, it may not always be practicable, or the most appropriate way of reporting on goods and services. The reporting on the cost of goods and services will depend on an entity's accounting policies and its cost allocation policies. If an entity reports on the cost of goods and services it shall provide a reconciliation between the expenses in the financial statements and the total goods and services costs reported in the service performance information. Where unrecognised goods or services in-kind are a significant component of producing goods and services, any cost information provided shall also acknowledge the use of these resources. PBE IPSAS 23 *Revenue from Non-Exchange Transactions* establishes requirements for the recognition of donated goods and services.

**Presentation**

29. **An entity shall clearly identify the service performance information presented in accordance with this Standard.**
30. An entity may find it helpful to present the information required by this Standard as answers to questions such as Who are we?, Why do we exist?, What did we do? and How did we perform?
31. This Standard does not prescribe the format of service performance information. Entities develop a format that best meets the information needs of their users. Information may, for example, be presented in the form of graphs, tables, narrative, infographics, explanatory comments in 'pop-up' boxes or similar.
32. An entity may cross reference the service performance information and the financial statements so that

## SERVICE PERFORMANCE REPORTING

users can assess the service performance information within the context of the financial statements.

33. In presenting service performance information in accordance with this Standard an entity may incorporate, by cross-reference, information outside the general purpose financial report. The use of cross-referencing is permitted subject to the following requirements.
  - (a) It is still possible to identify the complete set of service performance information presented in accordance with this Standard.
  - (b) Locating the information elsewhere enhances the understandability of the financial report as a whole and the service performance information remains understandable and fairly presented.
  - (c) The cross-referenced information is available to users of the service performance information on the same terms as the financial report and at the same time.
34. Incorporating service performance information by cross-reference enhances the understandability of the service performance information if it:
  - (a) Links related information together so that the relationships between items of information are clear; and/or
  - (b) Reduces duplication of information.
35. If an entity applies cross-referencing in accordance with paragraph 33, it shall:
  - (a) Disclose, together with the statement of compliance in accordance with paragraph 28 of PBE IPSAS 1 *Presentation of Financial Reports*, a list of cross-referenced information that forms part of a complete set of service performance information in accordance with this Standard;
  - (b) Depict cross-referenced information as being information prepared in accordance with this Standard (and audited if applicable);
  - (c) Make the cross-referencing direct and precise as to what it relates to; and
  - (d) Ensure cross-referenced information remains unchanged and available over time at the cross-referenced location. [added following comments received from R6]

### Comparative Information and Consistency of Reporting

36. Service performance information should provide users with a basis and context to compare an entity's service performance over time, and where appropriate, against planned performance or the performance of other entities. Consistency of reporting aids comparability and this Standard establishes requirements for consistent reporting. However, an entity's service performance activities and performance measures and/or descriptions may change over time. This Standard requires that an entity provide information about those changes.
37. **An entity shall report comparative information in respect of:**
  - (a) **The preceding period for all amounts and, where relevant, narrative and descriptive information, reported in the current period; and**
  - (b) **Planned performance, if required by PBE IPSAS 1.**
38. Comparative information shall be included for those performance measures and/or descriptions for which an amount is reported in the current period. Comparative information shall be included for narrative and descriptive information when it is relevant to an understanding of the current period's service performance information. Judgement is required in deciding when to provide comparative narrative and descriptive information.
39. PBE IPSAS 1 requires comparisons against planned performance if an entity has previously published general purpose prospective service performance information for the reporting period. PBE IPSAS 1 also requires explanations of major variances. An entity reporting against planned performance shall consider whether original levels of planned activity or revised plans provide the most relevant and useful information. Information about revisions to plans during the period may help explain variances between original plans and actual results.



## SERVICE PERFORMANCE REPORTING

40. **An entity shall report service performance information consistently. If an entity changes what it reports or how it reports its service performance information, it shall explain the nature of those changes and their effect on the current period's service performance information.**
41. There are a number of reasons why an entity might change what it reports or how it reports its service performance information. Possible reasons include changes in:
- (a) The nature of the entity's activities from the prior period or from what was planned;
  - (b) The descriptions of goods and services or the way in which they are aggregated;
  - (c) The performance measures and/or descriptions used; and
  - (d) The costing policies.
42. Changes to comparative information are permitted, but not required. If an entity chooses to restate prior period or budget comparatives it discloses the effect of the changes on that comparative information.
43. **An entity shall correct material prior period errors, in the first service performance information authorised for issue after the discovery of the errors, by restating the comparative information for any prior period(s) presented in which the error occurred and disclosing an explanation of the error. If the error relates solely to narrative information, an explanation of the error shall be disclosed. [added following comments received from respondent R6]**

**Disclosure of Judgements**

44. **An entity shall disclose information about the critical judgements made in the selection, measurement, aggregation and presentation of reporting service performance information reported in accordance with this Standard that are relevant to an understanding of the entity's service performance information. [Suggestions for consideration by NZASB and NZAuASB subcommittee members at meeting on 5 September 2017]**
45. In applying the principles in this Standard an entity will need to make a number of judgements, such as those discussed in paragraphs 19, 21 and 22. These judgements reflect the entity's consideration of its specific facts and circumstances, including the information needs of its primary users. Critical judgements are those that have the most significant effect on the selection, measurement and aggregation and presentation of service performance information. An entity therefore needs to identify critical judgements and consider the relevance of information about those judgements to a user's understanding of the entity's service performance information. [Suggestions for consideration by NZASB and NZAuASB subcommittee members at meeting on 5 September 2017]
46. In deciding what information about critical judgements to disclose in accordance with paragraph 44, an entity considers:
- (a) The extent to which the entity's service performance information is consistent with and clearly linked to the entity's overall purpose and strategies. If it is not, users may need to understand why not.
  - (b) The extent to which the entity's service performance information reported is consistent with that used by the entity for internal decision making. If it is not, users may need to understand why not.
  - (c) How much discretion the entity has over the selection, measurement and aggregation and presentation of service performance information. The more discretion the entity has over what it reports, the more users are likely to be interested in information about the entity's judgements. In situations where there is significant judgement involved, such disclosures shall include the key factors (see paragraph 19) that formed the basis of those judgements. In some cases an entity's service performance information might be largely determined by external requirements or agreements with external parties. In other cases an entity's service performance information might be largely determined internally, or it could be based upon a combination of internal determinations and external contractual determinations or frameworks. In all cases, information about the level of discretion that an entity has, and the judgements it has made, would be relevant to users seeking to understand the entity's service performance information. [Suggestions for



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consideration by NZASB and NZAuASB subcommittee members at meeting on 5 September 2017]

- (d) The extent to which the application of the qualitative characteristics and pervasive constraints (see paragraph 10) on information has influenced its service performance information. [added following comments received from R3 “we also believe some description of how materiality has been applied by preparers may also been required”]
  - (e) The extent to which consultation with users influenced the reporting of service performance information.
  - (f) The judgements made in deciding when to provide comparative narrative and descriptive information.
  - (g) In the case of service performance measures and/descriptions, the judgements made in relation to methodologies applied and key assumptions used. [added following comments received from R6]
- An entity may cross reference to other documents such as statements of intent or performance frameworks in disclosing information about critical judgements. [added following comments received from R6]

## Effective Date

47. **A public benefit entity shall apply this Standard for annual financial reports covering periods beginning on or after [Date – proposed 1 January 2021]. Earlier application is permitted.**

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**Amendments to Other Standards**

*An entity shall apply the amendments in this appendix when it applies PBE FRS XX issued in [Date].*

*The amendments to other standards in this appendix are based on the text of those other standards, including any amendments to those standards approved when PBE FRS XX was issued in [Date].*

*Amended paragraphs are shown with deleted text struck through and new text is underlined.*

**Generic amendments to PBE Standards  
(as a consequence of changing the title of PBE IPSAS 1)**

The title of PBE IPSAS 1 is changed from *Presentation of Financial Statements* to *Presentation of Financial Reports* in the following standards. Other generic amendments are as described below.

<b>Standard</b>	<b>Paragraph(s) amended</b>
PBE IPSAS 2 <i>Cash Flow Statements</i>	Paragraph 57
PBE IPSAS 3 <i>Accounting Policies, Changes in Accounting Estimates and Errors</i>	Paragraph 2 Paragraph 38, footnote
PBE IPSAS 4 <i>The Effects of Changes in Foreign Exchange Rates</i>	Paragraph 57
PBE IPSAS 5 <i>Borrowing Costs</i>	Paragraph 19, footnote
PBE IPSAS 9 <i>Revenue from Exchange Transactions</i>	Objective, footnote
PBE IPSAS 10 <i>Financial Reporting in Hyperinflationary Economies</i>	Paragraph 11
PBE IPSAS 11 <i>Construction Contracts</i>	Paragraph 16, footnote
PBE IPSAS 12 <i>Inventories</i>	Paragraph 16, footnote
PBE IPSAS 13 <i>Leases</i>	Paragraph 21, footnote Paragraph 78
PBE IPSAS 14 <i>Events After the Reporting Date</i>	Paragraph 16
PBE IPSAS 16 <i>Investment Property</i>	Paragraph 20, footnote
PBE IPSAS 17 <i>Property, Plant and Equipment</i>	Paragraph 14, footnote
PBE IPSAS 19 <i>Provisions, Contingent Liabilities and Contingent Assets</i>	Paragraph 19, footnote Paragraph A4
PBE IPSAS 20 <i>Related Party Disclosures</i>	Paragraph 22 Paragraph 38, footnote
PBE IPSAS 21 <i>Impairment of Non-Cash-Generating Assets</i>	Paragraph 37, footnote
PBE IPSAS 22 <i>Disclosure of Financial Information about the General Government Sector</i>	Paragraph 36, insert the title of PBE IPSAS 1
PBE IPSAS 23 <i>Revenue from Non-Exchange Transactions</i>	Paragraph 30, Paragraph 31, footnote Paragraph B9 Also, in paragraph B9 the reference to 'financial statements' is changed to 'financial report'.

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<b>Standard</b>		<b>Paragraph(s) amended</b>
PBE IPSAS 25	<i>Employee Benefits</i>	Paragraph 20, footnote Paragraph 26 Paragraph IE 6
PBE IPSAS 26	<i>Impairment of Cash-Generating Assets</i>	Paragraph 33, footnote
PBE IPSAS 27	<i>Agriculture</i>	Paragraph 13, footnote Paragraph 51
PBE IPSAS 28	<i>Financial Instruments: Presentation</i>	Paragraph 39, insert the title of PBE IPSAS 1 Paragraph AG53, insert the title of PBE IPSAS 1
PBE IPSAS 29	<i>Financial Instruments: Recognition and Measurement</i>	Paragraph 10, footnote Paragraph 64
PBE IPSAS 30	<i>Financial Instruments: Disclosures</i>	Paragraph 25, insert the title of PBE IPSAS 1 Paragraph 35, footnote In the final sentence of paragraph AG5, the reference to ‘financial statements’ is changed to ‘financial report’. In paragraph IG 3 the reference to ‘financial statements’ is changed to ‘financial statements or service performance information’.
PBE IPSAS 31	<i>Intangible Assets</i>	Paragraph 28, footnote
PBE IPSAS 32	<i>Service Concession Arrangements: Grantor</i>	Paragraph 31 Paragraph AG 20, footnote Paragraph AG49, insert the title of PBE IPSAS 1
PBE IPSAS 36	<i>Investments in Associates and Joint Ventures</i>	Paragraph 4, footnote Paragraph 16
PBE IPSAS 39	<i>Employee Benefits (forthcoming)</i>	Paragraph 25
PBE IFRS 3	<i>Business Combinations</i>	Paragraph 22, footnote
PBE IFRS 4	<i>Insurance Contracts</i>	Paragraph 20, footnote Paragraph 34 Paragraph C17.5.4
PBE IFRS 5	<i>Non-current Assets Held for Sale and Discontinued Operations</i>	Paragraph 3 Add footnote to title of PBE IPSAS 1 in paragraph BC6 which reads “PBE FRS XX <i>Service Performance Reporting</i> , issued in [Date], changed the title of PBE IPSAS 1 to <i>Presentation of Financial Reports</i> .”
PBE IFRS 9	<i>Financial Instruments</i>	Paragraph 5.6.5
PBE IAS 12	<i>Income Taxes</i>	Paragraph 14, footnote Paragraph 81(ab), insert title of

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Standard		Paragraph(s) amended PBE IPSAS 1
PBE FRS 46	<i>First-time Adoption of PBE Standards by Entities Previously Applying NZ IFRS</i>	Paragraph 18. Also, in paragraphs 18 and 20 the references to ‘financial statements’ are changed to ‘financial report’. Appendix A, paragraph 8, footnote
PBE FRS 47	<i>First-time Adoption of PBE Standards by Entities Other Than Those Previously Applying NZ IFRS</i>	Paragraph 28 Appendix C, paragraph C4, footnote
XRB A1	<i>Application of the Accounting Standards Framework</i>	Appendix C

**PBE IPSAS 1 Presentation of Financial Reports ~~Statements~~**

The title of PBE IPSAS 1 is changed from *Presentation of Financial Statements* to *Presentation of Financial Reports*. This change is made throughout the Standard.

Paragraphs 1–3, 7, 15–17, 19, 21, 24.1, 25–28.2, 28.4, 29, 31–33, 35–36, 38–39, 41–45, 46A, 47, 53–54, 59–66, 68–69, 78, 83, 85, 87, 116.1, 127–129, 131–134, 137–138, 144, 148A, 148C, 148.1–148.2 and 149–150 are amended. The headings above paragraphs 15, 19, 20.1, 61 and 148.1 are amended.

Paragraphs 20.1, 24.2 46A.1, 46A.2, 55.1, 126.1 (and a heading above that paragraph) and 154.9 are added.

Paragraphs 7.1, 18, and 150.1–150.10 (and the related heading), are deleted.

Appendix C is withdrawn.

New text is underlined and deleted text is struck through.

**Objective**

- The objective of this Standard is to prescribe the manner in which general purpose financial reports, comprising financial statements and, where required, service performance information,<sup>1</sup> should be presented to ensure comparability both with the entity’s financial ~~statements~~ reports of previous periods and with the financial ~~statements~~ reports of other entities. To achieve this objective, this Standard sets out overall considerations for the presentation of financial ~~statements~~ reports, guidance for their structure, and minimum requirements for the content of financial ~~statements~~ reports. The recognition, measurement, and disclosure of specific transactions and other events are dealt with in other PBE Standards.

<sup>1</sup> Reporting service performance information alongside the financial statements provides a comprehensive picture of an entity’s activities during the period. PBE FRS XX *Service Performance Reporting* specifies which entities are required to report service performance information in accordance with that Standard.

**Scope**

- This Standard shall be applied to all general purpose financial ~~statements~~ reports prepared and presented in accordance with PBE Standards.
- General purpose financial ~~statements~~ reports are those intended to meet the needs of users who are not in a position to demand reports tailored to meet their particular information needs. Users of general purpose financial ~~statements~~ reports include taxpayers and ratepayers, members of the legislature, donors, service recipients, creditors, suppliers, the media, and employees. General purpose financial ~~statements~~ reports include those that are presented separately or within another public document, such as an annual report. This Standard does not apply to condensed interim financial information (see PBE IAS 34 *Interim*

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*Financial Reporting*), prospective financial information (see PBE FRS 42 *Prospective Financial Statements*), or summary financial information (see PBE FRS 43 *Summary Financial Statements*).

...

## Definitions

7. The following terms are used in this Standard with the meanings specified:

**Material** Omissions or misstatements of items are material if they could, individually or collectively, influence the decisions or assessments of users made on the basis of the financial statements or service performance information. Materiality depends on the nature and size of the omission or misstatement judged in the surrounding circumstances. The nature or size of the item, or a combination of both, could be the determining factor.

**Notes** contain information in addition to that presented in the statement of financial position, statement(s) of comprehensive revenue and expense, statement of changes in net assets/equity, ~~and cash flow statement,~~ and service performance information. Notes provide narrative descriptions or disaggregations of items disclosed in those statements and information about items that do not qualify for recognition in those statements.

- 7.1 [Deleted by NZASB] ~~The following terms are used in this Standard with the meaning specified:~~

~~**Inputs** are the resources used to produce the goods and services which are the outputs of the entity.~~

~~**Outcomes** are the impacts on, or consequences for, the community resulting from the existence and operations of the entity.~~

~~**Outputs** are the goods and services produced by the entity.~~

## Purpose of Financial Statements ~~Reports~~

15. Financial ~~statements reports~~ are a structured representation of the financial position, and financial performance and service performance of an entity. The objectives of a general purpose financial statements report are to provide information about the financial position, financial performance, and cash flows, and service performance of an entity that is useful to a wide range of users in making and evaluating decisions about the allocation of resources. Specifically, the objectives of general purpose financial reporting should be to provide information useful for decision making, and to demonstrate the accountability of the entity for the resources entrusted to it, by:

- (a) Providing information about the sources, allocation, and uses of financial resources;
- (b) Providing information about how the entity financed its activities and met its cash requirements;
- (c) Providing information that is useful in evaluating the entity's ability to finance its activities and to meet its liabilities and commitments;
- (d) Providing information about the financial condition of the entity and changes in it; and
- (e) Providing aggregate information useful in evaluating the entity's performance in terms of service delivery, costs, efficiency, and accomplishments.

16. General purpose financial ~~statements reports~~ can also have a predictive or prospective role, providing information useful in predicting the level of resources required for continued operations, the resources that may be generated by continued operations, and the associated risks and uncertainties. Financial reporting may also provide users with information:

...

17. To meet these objectives, ~~the a financial statements report~~ provides information about an entity's:

- (a) Assets;
- (b) Liabilities;
- (c) Net assets/equity;
- (d) Revenue;
- (e) Expenses;

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- (f) Other changes in net assets/equity; ~~and~~
  - (g) Cash flows; ~~and~~
  - (h) Where required, service performance.
18. ~~[Deleted by NZASB] Although the information contained in financial statements can be relevant for the purpose of meeting the objectives in paragraph 15, it is unlikely to enable all these objectives to be met. This is likely to be particularly so in respect of entities whose primary objective may not be to make a profit, as managers are likely to be accountable for the achievement of service delivery as well as financial objectives. Supplementary information, including non financial statements, may be reported alongside the financial statements in order to provide a more comprehensive picture of the entity's activities during the period.~~

**Responsibility for Financial Statements Reports**

19. The responsibility for the preparation and presentation of financial ~~statements~~ reports varies across entities. In addition, an entity may draw a distinction between who is responsible for preparing the financial ~~statements~~ report and who is responsible for approving or presenting the financial ~~statements~~ report. Examples of people or positions who may be responsible for the preparation of the financial ~~statements~~ report of individual entities (such as government departments or their equivalent) include the individual who heads the entity (the permanent head or chief executive) and the head of the central finance agency (or the senior finance official, such as the controller or accountant-general). Examples of people or positions who may be responsible for the preparation of the financial ~~statements~~ report in the not-for-profit sector would be the chief executive officer, the Chairperson, the chief financial officer or the treasurer of the entity, who could be either employees or volunteers. Regardless of who prepares the financial ~~statements~~ report, the governing body is usually responsible for presenting ~~those~~ the financial ~~statements~~ report.

...

**Components of Financial Statements Reports**

**20.1 A complete financial report comprises:**

- (a) **A complete set of financial statements; and**
  - (b) **Service performance information in accordance with PBE FRS XX *Service Performance Reporting*, where this is required to be reported.**
21. **A complete set of financial statements comprises:**
- ...
- (f) **Notes to the financial statements, comprising significant accounting policies and other explanatory notes; and**
- ...

24.1 Where an entity presents a comparison, in the financial ~~statements~~ report, ...

**24.2 Where an entity presents a comparison, in the financial report, of prospective service performance information and actual service performance information, such a comparison shall be in accordance with the requirements of this Standard.**

25. Entities are encouraged to present additional information to assist users in assessing the performance of the entity, and its stewardship of assets, as well as making and evaluating decisions about the allocation of resources. This additional information may include ~~details about the entity's outputs and outcomes in the form of (a) performance indicators, (b) statements of service performance, (c) programme reviews, and (d) other reports by management about the entity's achievements over the reporting period.~~
26. Entities are also encouraged to disclose information about compliance with legislative, regulatory, or other externally-imposed regulations. When information about compliance is not included in the financial ~~statements~~ report, ...

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## Overall Considerations

### Fair Presentation and Compliance with PBE Standards

\*27. **Financial statements reports shall present fairly the financial position, financial performance, and cash flows, and service performance** of an entity. Fair presentation requires the faithful representation of the effects of transactions, other events, and conditions in accordance with the definitions and recognition criteria for assets, liabilities, revenue, and expenses set out in PBE Standards. The application of PBE Standards, with additional disclosures when necessary, is presumed to result in financial statements reports that achieve a fair presentation.

RDR 27.1 **Financial statements reports shall present fairly the financial position, financial performance and cash flows, and service performance** of a Tier 2 entity. Fair presentation requires the faithful representation of the effects of transactions, other events and conditions in accordance with the definitions and recognition criteria for assets, liabilities, revenue, and expenses set out in the PBE Standards. The application of PBE Standards Reduced Disclosure Regime (PBE Standards RDR), with additional disclosure when necessary, is presumed to result in financial statements reports that achieve a fair presentation.

\*28. **An entity whose financial statements report complies ~~comply~~ with Public Benefit Entity Standards (PBE Standards) shall make an explicit and unreserved statement of such compliance in the notes. Financial statements reports shall not be described as complying with PBE Standards unless they comply with all the requirements of PBE Standards.**

RDR 28.1 **A Tier 2 entity whose financial report complies ~~statements comply~~ with Public Benefit Entity Standards Reduced Disclosure Regime (PBE Standards RDR) shall make an explicit and unreserved statement of such compliance in the notes. Financial statements reports shall not be described as complying with PBE Standards RDR unless they comply with all the requirements of PBE Standards RDR.**

28.2 **An entity shall disclose in the notes:**

- (a) **The statutory basis or other reporting framework, if any, under which the financial statements report is ~~are~~ prepared;**
- (b) **A statement whether the financial statements and, where appropriate, service performance information have been prepared in accordance with generally accepted accounting practice (GAAP); and**

...

RDR 28.3 ...

28.4 **A number of entities have ~~are required by legislation to prepare~~ general purpose financial reporting requirements which refer to statements that comply with GAAP. The legislative definition of GAAP in the Financial Reporting Act 2013 refers to applicable financial reporting standards approved by the External Reporting Board, which include PBE Standards. PBE Standards include requirements and guidance specific to public benefit entities and provide reduced disclosures for entities that qualify to apply the Reduced Disclosure Regime. An entity asserting compliance with GAAP therefore needs to describe the financial reporting standards that have been applied by the entity in preparing its financial statements, and where appropriate, service performance information. For example:**

- (a) **An entity complying with Tier 1 Accounting Requirements would state: "The financial statements [and service performance information] have been prepared in accordance with PBE Standards"; and**
- (b) **An entity complying with Tier 2 Accounting Requirements would state: "The financial statements [and service performance information] have ...**

29. **In virtually all circumstances, a fair presentation is achieved by compliance with applicable PBE Standards. A fair presentation also requires an entity:**

...

- (c) **To provide additional disclosures when compliance with the specific requirements in PBE Standards is insufficient to enable users to understand the impact of particular transactions,**

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other events, and conditions on the entity's financial position, ~~and~~ financial performance and service performance.

31. In the extremely rare circumstances in which management concludes that compliance with a requirement in a Standard would be so misleading that it would conflict with the objective of financial ~~statements~~ reports set out in this Standard, the entity shall depart from that requirement in the manner set out in paragraph 32 if the relevant regulatory framework requires, or otherwise does not prohibit, such a departure.
32. When an entity departs from a requirement of a Standard in accordance with paragraph 31, it shall disclose:
  - (a) That management has concluded that the financial ~~statements~~ report presents fairly the entity's financial position, financial performance, ~~and~~ cash flows, and service performance;
  - (b) ...
  - (c) The title of the Standard from which the entity has departed, the nature of the departure, including the treatment that the Standard would require, the reason why that treatment would be so misleading in the circumstances that it would conflict with the objective of financial ~~statements~~ reports set out in this Standard, and the treatment adopted; and
  - (d) For each period presented, the financial impact of the departure on each item in the financial ~~statements~~ report that would have been reported in complying with the requirement.
33. When an entity has departed from a requirement of a Standard in a prior period, and that departure affects the amounts recognised in the financial ~~statements~~ report for the current period, it shall make the disclosures set out in paragraph 32(c) and (d).
- ...
35. In the extremely rare circumstances in which management concludes that compliance with a requirement in a Standard would be so misleading that it would conflict with the objective of financial ~~statements~~ reports set out in this Standard, but the relevant regulatory framework prohibits departure from the requirement, the entity shall, to the maximum extent possible, reduce the perceived misleading aspects of compliance by disclosing:
  - (a) The title of the Standard in question, the nature of the requirement, and the reason why management has concluded that complying with that requirement is so misleading in the circumstances that it conflicts with the objective of financial ~~statements~~ reports set out in this Standard; and
  - (b) For each period presented, the adjustments to each item in the financial ~~statements~~ report that management has concluded would be necessary to achieve a fair presentation.
36. For the purpose of paragraphs 31–35, an item of information would conflict with the objective of financial ~~statements~~ reports when it does not represent faithfully the transactions, other events, and conditions that it either purports to represent or could reasonably be expected to represent and, consequently, it would be likely to influence decisions made by users of financial ~~statements~~ reports. When assessing whether complying with a specific requirement in a Standard would be so misleading that it would conflict with the objective of financial ~~statements~~ reports set out in this Standard, management considers:
  - (a) Why the objective of financial ~~statements~~ reports is not achieved in the particular circumstances; and
  - (b) How the entity's circumstances differ from those of other entities that comply with the requirement. If other entities in similar circumstances comply with the requirement, there is a rebuttable presumption that the entity's compliance with the requirement would not be so misleading that it would conflict with the objective of the financial ~~statements~~ reports set out in this Standard.
- ...



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**Going Concern**

38. When preparing a financial ~~statements report~~, an assessment of an entity's ability to continue as a going concern shall be made. This assessment shall be made by those responsible for the preparation of the financial ~~statements report~~. Financial ~~statements reports~~ shall be prepared on a going concern basis unless there is an intention to liquidate the entity or to cease operating, or if there is no realistic alternative but to do so. When those responsible for the preparation of the financial ~~statements report~~ are aware, in making their assessment, of material uncertainties related to events or conditions that may cast significant doubt upon the entity's ability to continue as a going concern, those uncertainties shall be disclosed. When financial ~~statements reports~~ are not prepared on a going concern basis, that fact shall be disclosed, together with the basis on which the financial ~~statements report~~ is ~~are~~ prepared and the reason why the entity is not regarded as a going concern.
39. Financial ~~statements reports~~ are normally prepared on the assumption that the entity is a going concern and will continue in operation and meet its statutory obligations for the foreseeable future. In assessing whether the going concern assumption is appropriate, those responsible for the preparation of financial ~~statements reports~~ take into account all available information about the future, which is at least, but is not limited to, twelve months from the approval of the financial ~~statements report~~.
- ...
41. The determination of whether the going concern assumption is appropriate is primarily relevant for individual entities rather than for a government as a whole. For individual entities, in assessing whether the going concern basis is appropriate, those responsible for the preparation of the financial ~~statements report~~ may need to consider...

**Consistency of Presentation**

42. **The presentation and classification of items in the financial ~~statements report~~ shall be retained from one period to the next unless:**
- (a) **It is apparent, following a significant change in the nature of the entity's operations or a review of its financial ~~statements report~~, that another presentation or classification would be more appropriate having regard to the criteria for the selection and application of accounting policies in PBE IPSAS 3; or**
  - (b) **A PBE Standard requires a change in presentation.**
43. A significant acquisition or disposal, or a review of the presentation of the financial ~~statements reports~~, might suggest that the financial ~~statements report~~ needs to be presented differently. For example, an entity may dispose of a savings bank that represents one of its most significant controlled entities and the remaining economic entity conducts mainly administrative and policy advice services. In this case, the presentation of the financial ~~statements report~~ based on the principal activities of the economic entity as a financial institution is unlikely to be relevant for the new economic entity.
44. An entity changes the presentation of its financial ~~statements report~~ only if the changed presentation provides information that is faithfully representative and is more relevant to users of the financial ~~statements report~~, and the revised structure is likely to continue, so that comparability is not impaired. When making such changes in presentation, an entity reclassifies its comparative information in accordance with paragraphs 55 and 56.

**Materiality and Aggregation**

45. **Each material class of similar items shall be presented separately in the financial ~~statements report~~. Items of a dissimilar nature or function shall be presented separately, unless they are immaterial.**
- ...
- 46A. When applying this and other PBE Standards an entity shall decide, taking into consideration all relevant facts and circumstances, how it aggregates information in the financial ~~statements report~~, which includes the notes. An entity shall not reduce the understandability of its financial ~~statements report~~ by obscuring material information with immaterial information or by aggregating material items that have different natures or functions.

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- 46A.1 Materiality has an important role in guiding the selection of service performance information to be included in a financial report. This is particularly so when an entity delivers a wide range of goods and services.
- 46A.2 When making judgements about whether items of service performance information are material, the following should be considered:
- (a) The users of financial reports and their information needs;
  - (b) How the qualitative characteristics affect presentation and disclosure (for example, service performance information must be relevant, but the overall volume of information must also be accessible in order for it to be understandable);
  - (c) How the nature and size of items of information, judged in the surrounding circumstances, affect presentation and disclosure; and
  - (d) Where financial and non-financial information that is material should be presented and disclosed.
47. Some PBE Standards specify information that is required to be included in the financial statements, or elsewhere in the financial report, which include the notes. An entity need not provide a specific disclosure required by a PBE Standard if the information resulting from that disclosure is not material. This is the case even if the PBE Standard contains a list of specific requirements or describes them as minimum requirements. An entity shall also consider whether to provide additional disclosures when compliance with the specific requirements in PBE Standards is insufficient to enable users of financial reports statements to understand the impact of particular transactions, other events and conditions on the entity's financial position, and financial performance and, where appropriate, service performance.

...

**Comparative Information***Minimum Comparative Information*

53. **Except when a PBE Standard permits or requires otherwise, an entity shall present comparative information in respect of the preceding period for all amounts reported in the financial statements report. An entity shall include comparative information for narrative and descriptive information if it is relevant to an understanding of the current period's financial statements-report.**
- 53A. **An entity shall present, as a minimum, one statement of financial position with comparative information for the preceding period, one statement of comprehensive revenue and expense with comparative information for the preceding period, one cash flow statement with comparative information for the preceding period and one statement of changes in net assets/equity with comparative information for the preceding period, and related notes. PBE FRS XX sets out requirements for the reporting of comparative service performance information.**
54. In some cases, narrative information provided in the financial statements report for the preceding period(s) continues to be relevant in the current period. For example, an entity discloses in the current period details of a legal dispute, the outcome of which was uncertain at the end of the preceding period and is yet to be resolved, are disclosed in the current period. Users may benefit from the disclosure of information that the uncertainty existed at the end of the preceding period and from disclosure of information about the steps that have been taken during the period to resolve the uncertainty. PBE FRS XX notes that judgement is required in deciding when to provide comparative narrative and descriptive information.

...

- 55.1 PBE FRS XX permits, but does not require, changes to comparative information.

...

**Structure and Content****Introduction**

59. ... PBE IPSAS 2 sets out requirements for the presentation of a cash flow statement. PBE FRS XX sets out requirements for the reporting of service performance information.

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60. This Standard sometimes uses the term disclosure in a broad sense, encompassing items presented on the face of the (a) ... ~~and~~ (d) cash flow statement, and (e) within the service performance information, where this is required, as well as in the notes. Disclosures are also required by other PBE Standards. Unless specified to the contrary elsewhere in this Standard, or in another Standard, such disclosures are made either on the face of the statement of financial position, statement of comprehensive revenue and expense, statement of changes in net assets/equity or cash flow statement (whichever is relevant), within the service performance information, or in the notes.

**Identification of the Financial Statements Report**

61. The financial ~~statements~~ report shall be identified clearly, and distinguished from other information in the same published document.
62. PBE Standards apply only to financial statements, and ~~statements of~~ service performance information, and not to other information presented in an annual report or other document. ...
63. **Each component of the financial ~~statements~~ report shall be identified clearly. In addition, the following information shall be displayed prominently, and repeated when it is necessary for a proper understanding of the information presented:**
- ...
- (b) **Whether the financial ~~statements~~ report covers the individual entity or the economic entity;**
- (c) **The reporting date or the period covered by the financial ~~statements~~ report, whichever is appropriate to that component of the financial ~~statements~~ report;**
- ...
- (e) **The level of rounding used in presenting amounts in the financial ~~statements~~ report.**
64. The requirements in paragraph 63 are normally met by presenting page headings and abbreviated column headings on each page of the financial ~~statements~~ report. Judgement is required in determining the best way of presenting such information. For example, when the financial ~~statements~~ report is are presented electronically, separate pages are not always used; the above items are then presented frequently enough to ensure a proper understanding of the information included in the financial ~~statements~~ report.
65. Financial ~~statements~~ reports are often made more understandable by presenting information in thousands or millions of units of the presentation currency. This is acceptable as long as the level of rounding in presentation is disclosed and material information is not omitted.

**Reporting Period**

66. **Financial ~~statements~~ reports shall be presented at least annually. When an entity's reporting date changes and the annual financial ~~statements~~ report is are presented for a period longer or shorter than one year, an entity shall disclose, in addition to the period covered by the financial ~~statements~~ report:**
- ...
68. Normally, financial ~~statements~~ reports are consistently prepared covering a one-year period. However, for practical reasons, some entities prefer to report, for example, for a 52-week period. This Standard does not preclude this practice, because the resulting financial ~~statements~~ report is are unlikely to be materially different from ~~those~~ the report that would be presented for one year.

**Timeliness**

69. The usefulness of financial ~~statements~~ reports is impaired if they are not made available to users within a reasonable period after the reporting date. An entity should be in a position to issue its financial ~~statements~~ report within six months of the reporting date.
- ...

**Statement of Financial Position**

78. The operating cycle of an entity is the time taken to convert inputs or resources into the goods and services produced by an entity ~~outputs~~. For instance, governments transfer resources to public sector entities so that they can convert those resources into goods and services, or outputs, to meet the government's desired social, political, and economic outcomes. Similarly, many not-for-profit entities

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receive grants and donations for conversion into services or goods in pursuit of social policy outcomes. When the entity's normal operating cycle is not clearly identifiable, its duration is assumed to be twelve months.

...

83. An entity ...:

...

(b) An agreement to refinance, or to reschedule payments, on a long-term basis is completed after the reporting date and before the financial ~~statements~~ report is ~~are~~ authorised for issue.

85. When an entity breaches an undertaking under a long-term loan agreement on or before the reporting date, with the effect that the liability becomes payable on demand, the liability is classified as current, even if the lender has agreed, after the reporting date and before the authorisation of the financial ~~statements~~ report for issue, not to demand payment as a consequence of the breach. The liability is classified as current because, at the reporting date, the entity does not have an unconditional right to defer its settlement for at least twelve months after that date.

...

87. In respect of loans classified as current liabilities, if the following events occur between the reporting date and the date the financial ~~statements~~ report is ~~are~~ authorised for issue, those events qualify for disclosure as non-adjusting events in accordance with PBE IPSAS 14 *Events After the Reporting Date*:

...

### Statement of Comprehensive Revenue and Expense

...

**\*116.1 An entity shall disclose fees to each auditor or reviewer, including any network firm<sup>2</sup> [footnote omitted], separately for:**

- (a) **The audit or review of the financial ~~statements~~ report; and**
- (b) **All other services performed during the reporting period.**

### Service Performance Information

126.1 Service performance information provides users of financial reports with a basis to assess the service performance of the entity. PBE FRS XX specifies which entities are required to present service performance information in accordance with that Standard and sets out requirements for the reporting of service performance information and related disclosures.

### Notes

#### Structure

127. **The notes shall:**

- (a) **Present information about the basis of preparation of the financial ~~statements~~ report and the specific accounting policies used, in accordance with paragraphs 132–139;**
- (b) **Disclose the information required by PBE Standards that is not presented on the face of the statement of financial position, statement of comprehensive revenue and expense, statement of changes in net assets/equity, ~~or~~ cash flow statement, or within the service performance information; and**
- (c) **Provide additional information that is not presented on the face of the statement of financial position, statement of comprehensive revenue and expense, statement of changes in net assets/equity, ~~or~~ cash flow statement, or within the service performance information, but that is relevant to an understanding of any of them.**

128. **Notes shall, as far as practicable, be presented in a systematic manner. In determining a systematic manner, the entity shall consider the effect on the understandability and comparability of its financial ~~statements~~ report. Each item on the face of the statement of financial position, statement of comprehensive revenue and expense, statement of changes in net assets/equity, ~~and~~ cash flow**

SERVICE PERFORMANCE REPORTING

**statement, and within the service performance information shall be cross-referenced to any related information in the notes.**

129. Examples of systematic ordering or grouping of the notes include:
- (a) Giving prominence to the areas of its activities that the entity considers to be most relevant to an understanding of its service performance, financial performance and financial position, such as grouping together information about particular operating activities;
  - ...
131. Notes providing information about the basis of preparation of the financial ~~statements~~ report and specific accounting policies may be presented as a separate component of the financial ~~statements~~ report.

*Disclosure of Accounting Policies*

132. **An entity shall disclose its significant accounting policies comprising:**
- (a) **The measurement basis (or bases) used in preparing the financial ~~statements~~ report;**
  - ...
  - (c) **The other accounting policies used that are relevant to an understanding of the financial ~~statements~~ report.**
133. It is important for users to be informed of the measurement basis or bases used in the financial ~~statements~~ report (for example, historical cost, current cost, net realisable value, fair value, recoverable amount, or recoverable service amount), because the basis on which the financial ~~statements are~~ report is prepared significantly affects ~~their~~ its analysis. When more than one measurement basis is used in the financial ~~statements~~ report, for example when particular classes of assets are revalued, it is sufficient to provide an indication of the categories of assets and liabilities to which each measurement basis is applied.
134. In deciding whether a particular accounting policy should be disclosed, management considers whether disclosure would assist users in understanding how transactions, other events, and conditions are reflected in the reported financial performance and financial position. Each entity considers the nature of its operations and the policies that the users of its financial ~~statements~~ report would expect to be disclosed for that type of entity. ...
- ...
137. **An entity shall disclose, along with its significant accounting policies or other notes, the judgements, apart from those involving estimations (see paragraph 140), management<sup>2</sup> has made in the process of applying the entity's accounting policies that have the most significant effect on the amounts recognised in the financial ~~statements~~ report.**
- <sup>2</sup> In this context, management is the person/committee responsible for the financial ~~statements~~ report.
138. In the process of applying the entity's accounting policies, management makes various judgements, apart from those involving estimations, that can significantly affect the amounts recognised in the financial ~~statements~~ report. ...
- ...
144. The disclosures in paragraph 140 are presented in a manner that helps users of a financial statements report to understand the judgements management makes about the future and about other key sources of estimation uncertainty. ...

*Capital*

- \*148A. An entity shall disclose information that enables users of its financial ~~statements~~ report to evaluate the entity's objectives, policies, and processes for managing capital.
- ...
- \*148C. ... When an aggregate disclosure of capital requirements and how capital is managed would not provide useful information or distorts a financial ~~statement~~ report user's understanding of an entity's capital resources, the entity shall disclose separate information for each capital requirement to which the entity is subject.

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*Prospective Financial Statements and Prospective Service Performance Information*

148.1 Where an entity has published general purpose prospective financial statements or general purpose prospective service performance information for the period of the financial statements report, the entity shall present a comparison of the prospective financial statements report with the historical financial statements report being reported presented. Explanations for major variances shall be given.

148.2 PBE FRS 42 *Prospective Financial Statements* defines general purpose prospective financial statements and general purpose prospective service performance information. Legislative or other requirements may require a comparison with originally published information, the most recently published information, or both.

...

*Other Disclosures*

\*149. An entity shall disclose in the notes:

- (a) The amount of dividends, or similar distributions, proposed or declared before the financial statements ~~were report was~~ authorised for issue, but not recognised as a distribution to owners during the period, and the related amount per share; and

...

\*150. An entity shall disclose the following, if not disclosed elsewhere in information published with the financial statements report:

...

**Statement of Service Performance**

150.1–150.10 [Deleted.]

...

**Effective Date**

...

154.9 PBE FRS XX *Service Performance Reporting*, issued in [Date], amended paragraphs 1–3, 7, 15–17, 19, 21, 24.1, 25–28.2, 28.4, 29, 31–33, 35–36, 38–39, 41–45, 46A, 47, 53–54, 59–66, 68–69, 78, 83, 85, 87, 116.1, 127–129, 131–134, 137–138, 144, 148A, 148C, 148.1–148.2 and 149–150 and amended the headings above paragraphs 15, 19, 20.1, 61 and 148.1, added paragraphs 20.1, 24.2, 46A.1–46A.2, 55.1 and 126.1 and a heading above that paragraph, deleted paragraphs 7.1, 18, and 150.1–150.10 and the related heading, and withdrew Appendix C. An entity shall apply those amendments when it applies PBE FRS XX.

Paragraph BC3 is amended and paragraph BC4 is deleted. New text is underlined and deleted text is struck through.

**Service Performance Reporting**

BC3. When PBE IPSAS 1 was first issued it ~~includes~~ included non-integral implementation guidance on service performance reporting (as Appendix C), pending the development of a standard on service performance reporting. The NZASB issued PBE FRS XX *Service Performance Reporting* in [Date] and, as a consequence, withdrew the previous non-integral implementation guidance in Appendix C. At that time, the NZASB also made a number of changes to PBE IPSAS 1, including changing the title of that Standard to reflect the fact that the general purpose financial reports of many PBEs include both financial statements and service performance information. The NZASB noted that the change in title of PBE IPSAS 1 was for consistency between PBE Standards and the *Public Benefit Entities' Conceptual Framework* and did not imply that entities should change the title of their general purpose financial report. This guidance is based on that previously set out in *Technical Practice Aid 9 Service Performance Reporting* (New Zealand Institute of Chartered Accountants, 2007) (TPA 9). The NZASB noted that although TPA 9 was previously published in the handbook of Applicable Financial Reporting Standards it did not have authoritative support.

For consideration at the NZASB September 2017 meeting.

#### SERVICE PERFORMANCE REPORTING

BC4. ~~[Deleted by NZASB] The NZASB agreed, as a short term measure pending activation of a new project on performance reporting, to include guidance based on TPA 9 as non integral implementation guidance accompanying PBE IPSAS 1. In developing guidance to be incorporated in a standard, the NZASB agreed that the guidance should be appropriate for application by both public sector and not for profit (NFPs) entities. TPA 9 was focused on central and local government. In giving effect to this decision, the Board agreed that the guidance should acknowledge that NFPs may be providing goods and services on behalf of others or in order to further their own objectives and that the circumstances will determine the nature of their accountability to external parties.~~

Appendix C is withdrawn.

## Appendix C

### Service Performance Reporting

~~[Deleted by NZASB]~~

The Comparison with IPSAS 1 is amended as shown. New text is underlined and deleted text is struck through.

### Comparison with IPSAS 1

PBE IPSAS 1 *Presentation of Financial Reports ~~Statements~~* is drawn from IPSAS 1 *Presentation of Financial Statements*.

The significant differences between PBE IPSAS 1 and IPSAS 1 are:

- (a) The title of PBE IPSAS 1 reflects the fact that it establishes presentation requirements for both financial statements and service performance information.
- ~~(ba)~~ PBE IPSAS 1 reflects the New Zealand regulatory environment, including the requirements in the Financial Reporting Act 2013 regarding compliance with accounting standards. ~~It notes that an entity reporting in accordance with the Financial Reporting Act 1993 is not permitted to depart from the requirements of an accounting standard.~~
- ~~(cb)~~ PBE IPSAS 1 requires an assertion of compliance with PBE Standards rather than an assertion of compliance with IPSASs.
- ~~(de)~~ PBE IPSAS 1 requires the following additional disclosures:
  - (i) The statutory base or other reporting framework, if any, under which the financial statements are prepared;
  - (ii) The fact that the entity is a public benefit entity;
  - (iii) The fact that the financial statements comply with PBE Standards;
  - (iv) Whether the entity has availed itself of any disclosure concessions; and
  - (v) Fees paid to each auditor or reviewer, including any network firm, for the audit or review of the financial statements and all other services performed during the reporting period; ~~and~~
  - (vi) ~~Where a statement of service performance is presented, a description and disclosure of the outputs of the entity and the outcome(s) to which the outputs are intended to contribute.~~
- ~~(d)~~ ~~PBE IPSAS 1 includes non integral implementation guidance on service performance reporting.~~
- (e) PBE Standards require the presentation of a statement of comprehensive revenue and expense. IPSASs require the presentation of a statement of financial performance.
- (f) PBE IPSAS 1 includes illustrative financial statements for a not-for-profit entity.

## SERVICE PERFORMANCE REPORTING

**PBE IAS 34 *Interim Financial Reporting***

The Objective and paragraphs 4, 16A, 19, RDR 19.1, 23–25 and 25.2 (and the heading preceding 25.1) are amended. Paragraphs 25.1 and 25.3 are shown to provide context.

Paragraphs 8A.1, 9.1–9.3, 21.1, 25.1A and 49.10 are added.

Headings are added above paragraphs 9.1 and 21.1.

New text is underlined and deleted text is struck through.

**Objective**

The objective of this Standard is to prescribe the minimum content of an interim financial report and to prescribe the principles for recognition and measurement in complete or condensed financial statements and the requirements for presentation of service performance information for an interim period. Timely and faithfully representative interim financial reporting improves the ability of ~~users—investors, creditors, and others~~ to understand an entity's capacity to generate earnings and cash flows and its financial condition and liquidity. Where interim service performance information is presented, it improves the ability of users to make decisions about funding and assess accountability for use of resources on an ongoing basis.

4. **The following terms are used in this Standard with the meanings specified:**

...

**Interim financial report** means a financial report for an interim period containing either the information required in a complete set of financial statements report (as described in PBE IPSAS 1 *Presentation of Financial Reports Statements*) or a set of condensed financial report statements (as described in this Standard) for an interim period.

**Minimum Components of an Interim Financial Report**

...

**8A.1 An interim financial report may, but is not required to, include condensed service performance information.**

**Form and Content of Interim Service Performance Information**

**9.1 If an entity publishes a complete set of service performance information in its interim financial report, the form and content of that information shall conform to the requirements of PBE FRS XX *Service Performance Reporting*.**

**9.2 If an entity publishes condensed service performance information in its interim financial report, that information shall be presented in a manner consistent with the service performance information in the most recent annual financial report, or an explanation of the differences shall be provided.**

**9.3 Although the presentation of condensed service performance information will often involve the selection of a subset of service performance information, the performance measures and/or descriptions included in condensed service performance information should be as consistent as possible with those used in the annual financial report. Differences may occur due to changes in an entity's activities or an entity's decision to change the way in which it collects and reports information. This Standard requires disclosure of any differences.**

...

**Other Disclosures**

**16A. In addition to disclosing significant events and transactions in accordance with paragraphs 15–15C, an entity shall include the following information, in the notes to its interim financial statements or service performance information, or elsewhere in the interim financial report. The following disclosures shall be given either in the interim financial statements or incorporated by cross-reference from the interim financial statements to some other statement (such as management commentary or risk report) that is available to users of the financial statements on the same terms**



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as the interim financial statements and at the same time. If users of the financial statements do not have access to the information incorporated by cross-reference on the same terms and at the same time, the interim financial report is incomplete. The information shall normally be reported on a financial year-to-date basis.

- (a) A statement that the same accounting policies and methods of computation are followed in the interim financial statements and, where relevant, service performance information, as compared with the most recent annual financial statements or service performance information, or, if those policies or methods have been changed, a description of the nature and effect of the change.

...

- (h) Events after the interim period that have not been reflected in the financial statements or, where relevant, service performance information for the interim period.

## Disclosure of Compliance

- \*19. If an entity's interim financial report is in compliance with PBE IAS 34, that fact shall be disclosed. An interim financial report shall not be described as complying with PBE Standards unless the financial statements and the service performance information, if included, in that report comply with all of the requirements of PBE Standards.

RDR 19.1 If an entity's interim financial report is in compliance with this Standard as it applies to Tier 2 entities, that fact shall be disclosed. An interim financial report shall not be described as complying with PBE Standards Reduced Disclosure Regime (PBE Standards RDR) unless the financial statements and the service performance information, if included, in that report comply with all of the requirements of PBE Standards RDR.

...

## Periods for which Interim Service Performance Information may be Presented

- 21.1 Interim reports that include interim service performance information shall include service performance information (condensed or complete) for the current interim period and cumulatively for the current financial year to date, with comparative information for the comparable interim periods (current and year-to-date) of the immediately preceding financial year.

...

## Materiality

- 23. In deciding how to recognise, measure, classify, or disclose an item for interim financial reporting purposes, materiality shall be assessed in relation to the interim period ~~financial~~ data. In making assessments of materiality, it shall be recognised that interim measurements may rely on estimates to a greater extent than measurements of annual ~~financial~~ data.
- 24. PBE IPSAS 1 and PBE IPSAS 3 *Accounting Policies, Changes in Accounting Estimates and Errors* define an item as material if its omission or misstatement could influence the ~~economic~~ decisions or assessments of users of the financial statements or service performance information. PBE IPSAS 1 requires separate disclosure of material items, including (for example) discontinued operations, and PBE IPSAS 3 requires disclosure of changes in accounting estimates, errors and changes in accounting policies. The two Standards do not contain quantified guidance as to materiality.
- 25. While judgement is always required in assessing materiality, this Standard bases the recognition and disclosure decision on data for the interim period by itself for reasons of understandability of the interim figures. Thus, for example, unusual items, changes in accounting policies or estimates, and errors are recognised and disclosed on the basis of materiality in relation to interim period data to avoid misleading inferences that might result from non-disclosure. The overriding goal is to ensure that an interim financial report includes all information that is relevant to understanding an entity's financial position and performance, and where relevant, its service performance, during the interim period.

## Prospective Financial Statements and Prospective Service Performance Information

- 25.1 Where an entity has published general purpose prospective financial statements for the period of the interim financial statements, the entity shall present a comparison of the prospective financial

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statements with the historical financial statements being reported. Explanations for major variances shall be given.

**25.1A Where an entity publishes condensed service performance information in its interim financial report, and has previously published general purpose prospective service performance information for the period of the interim financial report, the entity shall present a comparison of the prospective service performance information with the historical information being reported. Explanations for major variances shall be given.**

25.2 PBE FRS 42 *Prospective Financial Statements* defines general purpose prospective financial statements and general purpose prospective service performance information. Legislative or other requirements may require a comparison with originally published information, the most recently published information, or both.

25.3 Comparison of prospective financial statements with actual financial results is an essential element of accountability. In the case of FMC reporting entities a comparison of actual financial results against the originally published prospective statements is important because it provides users with a comparison of actual performance with the projected performance at the time the entity raised funds. In the case of other entities, comparisons between projected performance and actual performance for a period are a means of demonstrating accountability for the resources used and the financial management of assets and liabilities. Some entities provide long-term prospective financial statements which are updated annually, prior to the beginning of the year. In such cases a comparison of actual financial results with the most recent prospective financial statements published prior to the beginning of the period is generally relevant. Where information is revised during the course of a year, the reasons for revising the information and an explanation of the differences between the originally published prospective financial statements and the historical financial statements should be given.

**Effective Date**

...

49.10 PBE FRS XX *Service Performance Reporting*, issued in [Date], amended the Objective, paragraphs 4, 16A, 19, RDR 19.1, 23–25, 25.2, added paragraphs 8A.1, 9.1–9.3, 21.1 and 25.1A, and added headings above paragraphs 9.1 and 21.1. An entity shall apply those amendments when it applies PBE FRS XX.

Paragraph BC8 is added.

**Service Performance Reporting**

BC8. PBE FRS XX *Service Performance Reporting*, issued in [Date], established requirements for public benefit entities to report service performance information. At that time the NZASB amended PBE IAS 34 *Interim Financial Reporting* to refer to both interim financial statements and interim service performance information. The NZASB left the decision as to whether to include service performance information in an interim financial report to the discretion of the entity. In doing so the NZASB acknowledged that there may be circumstances in which an entity is required to produce interim financial statements, and the users of that interim information may be interested solely in financial information.

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**PBE FRS 42 *Prospective Financial Statements***

[See issue 6 in agenda item 6.2. R6 recommended not making these changes to PBE FRS 42.](#)

The Introduction is amended.

New text is underlined and deleted text is struck through.

**Introduction**

General purpose prospective (future oriented or forward looking) financial statements and general purpose prospective service performance information are based on assumptions about the future and other information, and thus relate to events and actions which have not yet occurred. Although evidence may be available to support the assumptions on which the general purpose prospective financial statements or service performance information are based, such evidence is itself usually future oriented and therefore speculative in nature.

Given that anticipation of the future environment is associated with considerable uncertainty, the preparation of general purpose prospective financial statements and service performance information requires the exercise of significant judgement.

General purpose prospective financial statements and service performance information are less amenable to objective verification than historical data. When working with, or using, general purpose prospective statements and service performance information, it is essential to understand their inherent limitations.

**Main Features of the Standard**

PBE FRS 42 applies where an entity is required, or chooses, to present general purpose prospective financial information or general purpose prospective service performance information. Entities applying the Standard are required to present a complete set of general purpose prospective financial statements for the reporting period for which interim or annual historical general purpose financial statements will subsequently be presented.

The Standard requires that an entity use the best information that could reasonably be expected to be available in determining the assumptions and other information used in the preparation of general purpose prospective financial statements. ~~It also requires that~~ The prospective financial statements must be understandable, relevant, faithfully representative and comparable and ~~that~~ the information in the prospective financial statements must be reasonable and supportable. The Standard also requires that an entity presenting general purpose prospective service performance information present comprehensive information that is based on the assumptions and information consistent with that used to prepare any prospective financial information.

The assumptions used must:

- (a) Be based on the best information that could be reasonably expected to be available to the entity at the time prospective financial statements are prepared;
- (b) Be internally consistent among themselves;
- (c) Be consistent with the current plans of the entity to the extent that this is relevant;
- (d) Be applied consistently; and
- (e) Have a reasonable and supportable basis.

The Standard requires disclosure of:

- (a) The entity's operations and activities;
- (b) The purpose for which the prospective financial statements and prospective service performance information have been prepared;
- (c) Significant assumptions;
- (d) Any changes to the entity's existing operations;
- (e) The bases on which the significant assumptions have been prepared, including the principal sources of information from which they have been derived;

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- (f) The extent to which actual events and transactions have been reflected in the prospective financial statements and prospective service performance information;
- (g) The factors that may lead to a material difference between the prospective financial statements and prospective service performance information and the actual financial results and service performance information reported presented in historical financial statements in future reporting periods;
- (h) The assumptions made in relation to those sources of uncertainty and the potential financial effect of the uncertainty on the prospective financial statements and the potential effect of the uncertainty on prospective service performance information;

...

Paragraphs 1, 3, 6–10, 11.1, 12–19, 21–23, 25–27 and the heading preceding paragraph 26, 41–56 and the heading preceding paragraph 44, 58–69 and 70.1 are amended. Paragraph 64 is shown to provide context.

Paragraphs 27A, 27B, 64.1 and 73.3 are added.

New text is underlined and deleted text is struck through.

1. The objective of this Standard is to establish principles and specify minimum disclosures for entities that present general purpose prospective financial statements or general purpose prospective service performance information (hereafter referred to as ‘prospective financial statements’ and ‘prospective service performance information’ except where otherwise stated). To provide users with high quality general purpose prospective financial information, this Standard requires that an entity presenting general purpose prospective financial information present a complete set of prospective financial statements using the best information that could reasonably be expected to be available and which meet certain qualitative characteristics. This Standard also requires that an entity presenting general purpose prospective service performance information present comprehensive information that is based on the assumptions and information consistent with that used to prepare any prospective financial information.

...

3. An entity shall apply this Standard where it is required, or chooses, to present general purpose prospective financial information or general purpose prospective service performance information.

...

6. Examples of prospective information to which this Standard does not apply include:
  - (a) Special purpose prospective financial information;
  - (b) Prospective information expressed solely in general terms; and
  - (c) Prospective non-financial information, other than the prospective service performance information discussed in this Standard.

Nonetheless application of the principles and requirements of this Standard to prospective ~~financial~~ information outside the scope of this Standard is encouraged to the extent applicable.

7. Special purpose prospective ~~financial~~ information is prepared for external users who are able to require, or contract for, the preparation of special reports to meet their specific information needs. It may be prepared in a form agreed to by the parties.
8. Prospective information which is expressed solely in general terms includes qualitative statements about future prospects. Such statements are commonly found in:
  - (a) Narrative commentary within an entity’s financial report; and
  - (b) Commentary in statements of intent provided by government departments and Crown entities and in long-term plans provided by local authorities.

However, the above information, where presented, should be consistent with any current published prospective financial statements and prospective service performance information.

## SERVICE PERFORMANCE REPORTING

9. Prospective non-financial information includes forward-looking disclosures about an entity's objectives, activities and performance targets. Non-financial information is often provided because financial information alone is unlikely to meet all the needs of users. In the case of public sector entities, legislation may require the publication of prospective non-financial information ~~such as objectives, nature and scope of activities and performance targets in relation to objectives, outputs or outcomes. Some non-financial information will be prospective information that falls within the scope of this Standard.~~ Where non-financial and financial information ~~are~~ published together they should be consistent.
10. **A public benefit entity whose prospective financial statements, and prospective service performance information where this is provided, comply with PBE FRS 42 shall make an explicit and unreserved statement of such compliance in the notes. Prospective financial statements and prospective service performance information shall not be described as complying with PBE FRS 42 unless they comply with all the requirements of PBE FRS 42.**
- ...
- 11.1 **The following terms are used in this Standard with the meanings specified:**
- ...
- General purpose prospective service performance information means future-oriented service performance information prepared for external users who are unable to require, or contract for, the preparation of special reports to meet their specific information needs.**
12. Prospective financial statements and prospective service performance information prepared using the principle of best information, that are reasonable and supportable, and that meet the qualitative characteristics outlined in paragraphs 16 and 17 of this Standard are likely to be of a high quality and assist users in forming, revising or confirming their expectations about the future.
13. **An entity shall use the best information that could reasonably be expected to be available at the time prospective financial statements and prospective service performance information are prepared in determining the assumptions and information used in the preparation of the prospective financial statements and prospective service performance information.**
14. **The information in prospective financial statements and prospective service performance information shall be reasonable and supportable and faithfully represent the assumptions and information on which the financial statements and service performance information are based.**
15. ~~Prospective~~ The information in ~~prospective financial statements~~ is, by definition, uncertain and its preparation requires the exercise of judgement. Events and circumstances may not occur as expected or may not have been predicted. In addition, the entity may subsequently take actions which differ from the proposed courses of action on which the prospective information is ~~financial statements are~~ based. In seeking to demonstrate that ~~the prospective information in the prospective financial statements~~ is reasonable and supportable, an entity considers whether:
- (a) The course of action reflected in the prospective information ~~financial statements~~ represents the entity's proposed course of action, or, where alternative scenarios are presented, that those scenarios are feasible;
  - (b) It has a reasonable and supportable basis for the determination of assumptions underlying the prospective information ~~financial statements~~. Ways in which an entity can demonstrate that it has a reasonable and supportable basis for the assumptions underlying the prospective information ~~financial statements~~ are discussed in paragraphs 20 and 21; and
  - (c) It has used appropriate information.

**Qualitative Characteristics**

16. **In order to meet the needs of users, prospective financial statements and prospective service performance information shall meet the qualitative characteristics outlined in the *Public Benefit Entities' Conceptual Framework*. Accordingly, the statements and information shall be relevant, faithfully representative, understandable, timely, comparable and verifiable.**

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17. In giving effect to the principle in paragraph 16, for prospective financial statements and prospective service performance information to be:
- (a) **Relevant**—the information in the statements and service performance information should be capable of assisting users to make economic or other decisions by helping them evaluate present or future events or correct their past evaluations. For prospective financial statements and service performance information to be relevant they must have predictive value and be able to be confirmed, or otherwise, in future periods.
  - (b) **Faithfully Representative**—the information in the statements and service performance information should be complete, neutral, and free from material error. The extent to which prospective financial statements and service performance information can be described as faithfully representative is affected by the appropriateness of the assumptions and the sources of uncertainty. Users should be able to assess the extent to which prospective financial statements and service performance information are faithfully representative and identify the factors that make the statements and service performance information more or less faithfully representative.
  - (c) **Understandable**—the information ~~in the statements~~ should be described, aggregated, classified and presented in a format and style that is able to be clearly understood by users. For prospective financial statements and service performance information to be understandable, users will need sufficient information to be able to make judgements about the assumptions employed and the risks associated with those assumptions.
  - (d) **Timely**—the information should be reported to users before it loses its capacity to be useful for accountability and decision-making purposes.
  - (e) **Comparable**—the statements should measure and display like items, transactions and events in a consistent manner. Service performance information should be presented as consistently as possible over time. Prospective financial statements and service performance information should be capable of comparison with current and subsequent information about the actual ~~financial~~ performance of an entity based on consistent application of accounting policies, reporting periods and presentation.
  - (f) **Verifiable**—the statements and service performance information should be transparent about the assumptions that underlie the information disclosed, the methodologies adopted in compiling that information, and the factors and circumstances that support any opinions expressed or disclosures made.

## Assumptions

18. **Assumptions shall be based on the best information that can reasonably be expected to be available to the entity, be consistent among themselves, be consistent with the current plans of the entity to the extent that this is relevant, and be applied consistently. An entity shall have a reasonable and supportable basis for the determination of assumptions underlying prospective financial statements and service performance information.**
19. An assumption is a view taken about the future for the purpose of preparing prospective information ~~financial statements~~. Assumptions are taken as being true for the purpose of preparing prospective information ~~financial statements~~ but could change later. An assumption is made where some facts are not yet known or decided. In preparing prospective information ~~financial statements~~ an entity generally needs to make assumptions regarding economic and business conditions and proposed courses of action. For example, an entity may assume that the nature of its operations and principal activities for the period of the prospective financial statements and prospective service performance information will be consistent with the operations and activities outlined in certain plans and strategies of the entity. Information used in the preparation of prospective information ~~financial statements~~ may include the current plans and strategies of the entity, some of which may be published, market surveys, industry statistics, economic and other indicators or specialised studies.
- ...
21. Where prospective financial statements and prospective service performance information present information on activities that have no track record and that are not subject to considerable management control and discretion, it is more difficult to establish that there is a reasonable and supportable basis for

# SERVICE PERFORMANCE REPORTING

the assumptions. Ways in which an entity preparing prospective financial statements and prospective service performance information in a start-up situation can demonstrate a reasonable and supportable basis for the assumptions include:

...

- (c) Detailed analysis by area of activity (for example, goods and services by type market, product line or geography and cost by function);
22. Assumptions are frequently interdependent. An assumption may affect many items within prospective financial statements and prospective service performance information and lead to the formulation of other assumptions. Where assumptions are interdependent, the treatment of the interdependent assumptions in prospective financial statements and prospective service performance information should be consistent. For example, an entity may have a capital project that will need to be funded during the period of the prospective financial statements. As such, assumptions will be required about the source of the funding and the interest rates related to the funding. It may also be necessary to make assumptions about the related increase in depreciation charges.
23. Application of the principle of best information and the manner in which an entity demonstrates that it has a reasonable and supportable basis for assumptions will depend on the circumstances in which an entity prepares prospective financial statements and prospective service performance information. Prospective financial statements and prospective service performance information reflect an entity's assumptions regarding its proposed courses of action for the period of the prospective information financial statements. An entity may propose to continue its current operations and activities, make some changes to its current operations and activities, or engage in one or more alternative scenarios.
- (a) To the extent that an entity intends to continue its current operations and activities for the period of the prospective information financial statements, application of the best information principle requires that the assumptions and information used in the preparation of the prospective information financial statements be based on and consistent with the assumptions in the entity's current plans and strategies, updated as appropriate for more recent information forecasts of economic and business conditions.
  - (b) Where the nature of an entity's operations and its principal activities are expected to change significantly over the period of the prospective information financial statements, the assumptions will need to reflect these changes. Application of the best information principle in these circumstances requires that the assumptions and information used in the preparation of the prospective information financial statements reflect the entity's proposed course(s) of action, including any alternative scenarios, and the risks and uncertainties that inevitably surround many of the events and circumstances associated with those actions or scenarios. In such circumstances the assumptions and information used in the prospective information financial statements may be consistent with those in the entity's current plans and strategies, but only to the extent that those assumptions and information are relevant to the entity's planned actions or alternative scenarios. The quality of such prospective information financial statements is enhanced if it is they are supported by an analysis of the entity's current operations and the way in which those operations are expected to change under the proposed course of action, including any alternative scenarios.
- ...
25. Full disclosure of significant assumptions is essential in order for users to determine the extent to which they wish to rely on the information in prospective financial statements and prospective service performance information. Users require information about the assumptions used so they can make an informed judgement on the degree of reliability of the information in the prospective financial statements and prospective service performance information. Users also require information which assists them in assessing the sensitivity of information in prospective financial statements and prospective service performance information to changes in assumptions and the extent to which they are subject to a high degree of uncertainty.

## Prospective Financial Reporting

### Presentation of Prospective Financial Statements

26. An entity that presents prospective financial statements shall present and disclose information that enables users of those statements to evaluate the entity's financial prospects and to subsequently

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assess actual financial results ~~prepared in future reporting periods~~ against the prospective financial statements. An entity that also presents prospective service performance information shall present and disclose information that enables users of that information to evaluate the entity's proposed service performance and to subsequently assess actual service performance against the prospective service performance information.

27. Information presented on the face of prospective financial statements is usually presented as a line item. However, additional disclosures may be used to present information on the possible range for an individual item. When a range is used the band shall not be so broad as to render the information meaningless to users and the assumptions used shall be clearly linked to the upper and lower limits of the range. Where prospective financial information has a high level of uncertainty associated with it, a range is more likely to present useful information. Prospective service performance information may also be presented as a range for the same reasons.
- 27A. An entity's prospective service performance information shall include sufficient information to enable a reader to obtain a broad understanding of the projected service performance of the entity in a manner that is neither misleading nor biased. Consistent with the requirements of PBE FRS XX *Service Performance Reporting* it shall include contextual information about the entity, an appropriate and meaningful mix of performance measures and/or descriptions and critical judgements made in reporting prospective service performance information that are relevant to an understanding of that information. An entity's prospective service performance information shall be presented in a manner consistent with how the entity expects to report that information in the future.
- 27B The presentation of prospective service performance information will often involve the selection of a subset of the information that an entity would present in accordance with PBE FRS XX. Differences between the most recently reported service performance information and prospective service performance information may occur due to changes in an entity's activities or the way in which it collects and reports information.
- ...
41. Prospective financial statements and prospective service performance information shall be prepared in accordance with the accounting policies expected to be used in the future for reporting historical general purpose financial reports statements.
42. Where an entity presents both controlling entity and group financial statements for general purpose historical financial reporting, it should consider whether both controlling entity and group prospective financial statements should be presented. Similar considerations arise in respect of prospective service performance information. Factors to consider include the purpose and relevance of the prospective ~~financial~~ statements and information and whether, in the absence of group ~~prospective financial~~ statements and information, the statements and information ~~that are~~ presented in respect of the controlling entity would meet the qualitative characteristics set out in paragraphs 16 and 17 of this Standard.
43. Where an entity presents prospective financial statements and prospective service performance information in respect of the reporting entity for general purpose financial reporting and/or a subset of that reporting entity:
  - (a) The prospective financial statements and prospective service performance information for the reporting entity for which general purpose financial reports will subsequently be prepared shall be prepared in accordance with the accounting policies expected to be used in the future for ~~reporting~~ historical general purpose financial reports statements; and
  - (b) The prospective financial statements and prospective service performance information for the sub-entity shall be prepared in accordance with the accounting policies expected to be used in the future for ~~reporting~~ historical general purpose financial reports statements except where regulations otherwise require.



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**Periods Covered by Prospective Financial Reports Statements**

44. The reporting periods covered by prospective financial statements and prospective service performance information shall coincide with those for which interim or annual historical general purpose financial reports statements will subsequently be presented.
45. Where legislation or regulation require prospective financial information or prospective service performance information to be prepared for a reporting period which differs from the period for which historical general purpose ~~financial statements~~ or information will subsequently be presented, an entity is compelled to comply with such legislation or regulation. However, in such cases the entity may be able to comply with both this Standard and the relevant legislation or regulation by presenting prospective ~~financial~~ information for the balance of the current reporting period and for the subsequent interim or annual reporting period. Comparative requirements in relation to prospective ~~financial~~ information presented in historical financial reports statements are found in PBE IPSAS 1 *Presentation of Financial Reports Statements* and PBE IAS 34 *Interim Financial Reporting*.
46. The number of reporting periods covered by prospective financial reports statements may vary considerably depending on the relevant legal requirements and the purpose and objective for which the prospective financial reports statements are prepared. In general, the greater the number of future reporting periods included in prospective financial reports statements, the more unreliable and uncertain the information in the prospective financial reports statements becomes. Entities should exercise caution about publishing prospective financial statements and prospective service performance information for periods beyond that required by legislation or regulation. Entities publishing prospective financial statements and prospective service performance information, other than those required to publish prospective financial information and prospective service performance information by legislation or regulation, should exercise caution in presenting prospective financial statements and prospective service performance information for more than one reporting period.

**Disclosure****Disclosure of Operations and Activities**

47. An entity shall disclose the following, if not disclosed elsewhere in information published with the prospective financial report statements:
- (a) A description of the nature of the entity's current operations and its principal activities; and
  - (b) A description of the nature of the entity's operations and its principal activities for the period of the prospective financial report statements.

**Disclosure of the Purpose of Prospective Financial Reports Statements**

48. When a prospective financial report statements ~~is are~~ presented, the purpose for which it has ~~they have been~~ prepared shall be disclosed together with a caution that the information ~~in those statements~~ may not be appropriate for purposes other than those described.

**Disclosure of Bases for Assumptions, Risks and Uncertainties**

49. Prospective financial statements and prospective service performance information shall contain the information necessary for a user to appreciate the degree of uncertainty attaching to those statements and that ~~the information in those statements~~ and the impact of that uncertainty.

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50. The requirement that prospective financial statements and prospective service performance information contain the information necessary for a user to appreciate the degree of uncertainty attaching to the information in those statements and that information and the impact of that uncertainty requires the disclosure of assumptions, the risks associated with those assumptions, and other matters and information which are of importance to users' understanding of the prospective financial information statements. Disclosure of the risks surrounding assumptions and the potential impact of a change in an assumption on the prospective financial information statements enables users to assess the degree of uncertainty inherent in the ~~information in the prospective information financial statements~~ and the reliance they wish to place on ~~the that information in those statements~~. Such disclosure reduces the possibility that unwarranted credibility may be attached to the information. In forming a judgement on what constitutes reasonable disclosure, an entity will need to take into consideration:
  - (a) Sources of uncertainty and the assumptions made relating to uncertainties;
  - (b) The factors that will affect whether assumptions will be borne out in practice; and
  - (c) Alternative results, being the consequences of assumptions not being borne out.
51. **All significant assumptions underlying prospective financial statements and prospective service performance information shall be disclosed separately and clearly identified in a manner that makes their significance understandable to users. Where possible, assumptions shall be quantified.**
52. A significant assumption is one that materially affects one or more financial estimates or estimates relating to planned activities. One way of highlighting the significance of assumptions is to rank assumptions in order of importance in relation to their impact on the prospective information-financial statements. For example, the most significant risks may be uncertainty regarding the level of demand for a new product, exposure to future price changes (inflation), exposure to movements in foreign currency exchange rates or interest rates, and increased demand for services caused by shifts in population growth. If the level of expected demand for the new product is the most important assumption it should be disclosed as such and the risk of demand being significantly less than assumed should be disclosed as a key risk.
53. **Where prospective financial statements and prospective service performance information are not based on the entity's existing activities, this fact shall be disclosed together with a description of the changes proposed.**
54. Where prospective financial statements and prospective service performance information reflect planned actions or alternative scenarios that do not represent the entity's existing activities, this fact shall be disclosed to enable users to understand the nature of the changes proposed and the possible future direction that the entity may take.
55. **An entity shall disclose:**
  - (a) **The bases on which the significant assumptions have been prepared, including the principal sources of information from which they have been derived;**
  - (b) **The extent to which actual events and transactions have been reflected in the prospective financial statements and prospective service performance information;**
  - (c) **The factors that may lead to a material difference between information in the prospective financial statements and prospective service performance information, and the actual financial results and service performance reported ~~prepared~~ in future reporting periods; and**
  - (d) **The assumptions made in relation to those sources of uncertainty and the potential financial effect of the uncertainty on the prospective financial statements, and the potential effect of the uncertainty on prospective service performance information.**
56. The purpose of disclosure of the bases for the assumptions is to provide users with information to determine the extent to which they can rely on the information in the prospective financial statements and prospective service performance information. Disclosure about the bases of the preparation of the significant assumptions may include discussion of the process used to develop assumptions, including the use of documents such as plans, surveys and reports. The factors outlined in paragraph 20 and, where applicable, paragraph 21, are examples of items that could have formed the bases of assumptions.

## SERVICE PERFORMANCE REPORTING

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58. Examples of factors that may lead to a material difference between prospective financial statements and prospective service performance information and actual financial results and service performance include macroeconomic exposures, political changes, market volatility, competitor action and risks associated with the entity's own processes for producing goods and services. One way in which information on the effect of such uncertainties on prospective financial statements and prospective service performance information may be presented is a sensitivity analysis. Where a sensitivity analysis using positive or optimistic variables is presented, it should generally be accompanied by a corresponding analysis based on negative or pessimistic variables.
59. **Prospective financial statements and prospective service performance information shall include a cautionary note to the effect that actual financial results and service performance achieved for the period covered are likely to vary from the information presented, and that the variations may be material.**

**Disclosure of Accounting Policies**

60. **Significant accounting policies used as a basis for the preparation of prospective financial statements and prospective service performance information shall be disclosed in accordance with PBE IPSAS 1 *Presentation of Financial Statements*.**
61. **Where prospective financial statements or prospective service performance information give effect to a change in accounting policy, this change shall be disclosed, including the reason for the change and its effect on the prospective financial statements or prospective service performance information.**
62. The changes in accounting policies referred to in paragraph 61 include changes from the accounting policies used in the prior period historical general purpose financial ~~reports~~ statements and changes from the accounting policies used in prior period prospective financial statements where prospective financial statements are presented for more than one year.
63. **Where an entity publishes both controlling entity and group financial statements for historical financial reporting purposes but does not publish group prospective financial statements, it shall disclose the reasons for not presenting group prospective financial statements. Similarly, where an entity publishes both historic controlling entity and group service performance information but does not publish group prospective service performance information, it shall disclose the reasons for not presenting group prospective service performance information.**
64. **Where an entity publishes prospective financial statements in respect of a subset of a reporting entity in accordance with paragraph 43 it shall disclose:**
- (a) The reasons for presenting prospective financial statements for the subset; and
  - (b) Whether the entity intends to publish historical financial statements for the subset of the reporting entity for the period or periods covered by the prospective financial statements.
- 64.1 Where an entity publishes prospective service performance information in respect of a subset of a reporting entity in accordance with paragraph 43 it shall disclose:**
- (a) The reasons for presenting prospective service performance information for the subset; and**
  - (b) Whether the entity intends to publish historical service performance information for the subset of the reporting entity for the period or periods covered by the prospective service performance information.**

**Other Disclosures**

65. **When an entity presents prospective financial statements and prospective service performance information, it shall disclose:**
- (a) **The date when the prospective financial statements and prospective service performance information were authorised for issue and who authorised the issue of the prospective financial statements and prospective service performance information;**

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- (b) **A statement that the person or body that authorised the issue of the prospective financial statements and prospective service performance information by the entity is responsible for the prospective financial statements and prospective service performance information presented, including the appropriateness of the assumptions underlying the prospective financial statements and prospective service performance information and all other required disclosures;**
  - (c) **The extent to which actual financial results and service performance are incorporated and the period covered by those results; and**
  - (d) **Whether or not it is intended to update the prospective financial statements and prospective service performance information subsequent to presentation and, if so, when.**
66. The process involved in authorising the prospective financial statements and prospective service performance information for issue will vary depending upon the management structure, statutory requirements and procedures followed in preparing and finalising the prospective financial statements and prospective service performance information. It is important for users to know when the prospective financial statements and prospective service performance information were authorised for issue because this is the date of adoption of the underlying assumptions. The prospective financial statements and prospective service performance information do not reflect events or knowledge obtained after this date.
67. The authorising body is responsible for ensuring that the entity has a robust process for developing assumptions and that the assumptions developed are appropriate in the circumstances. The responsibility of the authorising body extends beyond ensuring that individual assumptions used to prepare the prospective financial statements and prospective service performance information are appropriate in the circumstances, to ensuring that the assumptions taken as a whole are appropriate and that there is adequate disclosure of all significant risks.
68. Disclosure of the date of adoption of the underlying assumptions alerts users to the possibility that events occurring subsequent to this date may affect the usefulness of the information presented. Disclosure of the extent to which actual financial results and service performance are incorporated and the period covered by those results provides an indication of the degree of reliability that can be attached to the information in the prospective financial statements and prospective service performance information. Further disclosure of whether or not it is intended to update the prospective financial statements and prospective service performance information subsequent to presentation may alert the user to the extent of the intention to communicate such updated information.

**Disclosure of Reasons for Revising Prospective Financial Statements and Prospective Service Performance Information**

69. **Where revised prospective financial statements and prospective service performance information are issued, the following shall be disclosed:**
- (a) **The reasons for revising the prospective financial statements and prospective service performance information;**
  - (b) **An explanation of the changes made to the prospective financial statements and prospective service performance information most recently issued, including a reconciliation of material differences between the previously reported prospective financial statements and prospective service performance information and the revised prospective financial statements and prospective service performance information; and**
  - (c) **The date as at which the prospective financial statements and prospective service performance information were revised.**
- ...
- 70.1 PBE IPSAS 1 specifies requirements for comparisons of actual financial information results ~~and actual service performance information~~ to prospective financial statements and prospective service performance information.

For consideration at the NZASB September 2017 meeting.

## SERVICE PERFORMANCE REPORTING

### Effective Date

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73.3 PBE FRS XX *Service Performance Reporting*, issued in [Date], amended paragraphs 1, 3, 6–10, 11.1, 12–19, 21–23, 25–27 and the heading preceding paragraph 26, 41–56 and the heading preceding paragraph 44, 58–69 and 70.1 and added paragraphs 27A, 27B and 64.1. An entity shall apply those amendments when it applies PBE FRS XX.

Paragraphs BC5 and BC6 are added. New text is underlined.

### Service Performance Reporting

BC5. PBE FRS XX *Service Performance Reporting*, issued in [Date], established requirements for public benefit entities to report service performance information. At that time the NZASB amended a number of other standards, including PBE FRS 42 *Prospective Financial Statements*. The amendments to PBE FRS 42 broaden the application of the Standard to prospective service performance information. The NZASB decided not to mandate the presentation of service performance information in conjunction with all prospective financial statements on the grounds that there may be some situations in which it is appropriate for an entity to present prospective financial statements without also presenting prospective service performance information.

BC6. The NZASB also considered whether the title of PBE FRS 42 should be changed to *Prospective Financial Reports* to signal that the Standard contains requirements for both financial statements and service performance information. The NZASB decided not to change the title of PBE FRS 42 at this time as it did not anticipate that the [2017] amendments would change current practice regarding when prospective service performance information is presented with prospective financial statements. The NZASB noted that it had a separate project underway to review the requirements in PBE FRS 42 and that any change in title could be considered in the context of that project.

## PBE FRS 43 *Summary Financial Statements*

Paragraphs 9, 11A, 11B, 12 and the preceding heading, and paragraph 16 are amended.

Paragraph 44.4 is added.

New text is underlined and deleted text is struck through.

9. **Summary financial statements shall include a summary of each financial statement included in a full financial report. If the full financial report included service performance information, summary financial statements shall be accompanied by a summary of that service performance information. ~~If the full financial report is required to include non-financial statements such as a statement of service performance, the summary financial statements shall be accompanied by a summary of the non-financial statements required to be included in the full financial report.~~**

...

### Application of Materiality

11A. **An entity shall disclose sufficient information in its summary financial statements and summary service performance information to enable a reader to obtain a broad understanding of the financial position and performance, and service performance, of the entity in a manner that is neither misleading nor biased.**

11B. The disclosures required by this Standard are subject to the definition of materiality in PBE IPSAS 1 *Presentation of Financial ~~Statements~~ Reports*. They shall be disclosed separately if they are of such incidence and size, or of such nature, that their disclosure is necessary to explain the performance or financial position of the entity. A summary description of each material item, as included in the most recent full financial statements, shall be given to enable its nature to be understood. A summary description of items relating to other periods covered by the summary shall be given where this is required for an understanding of the summary financial statements, taken as a whole.

For consideration at the NZASB September 2017 meeting.

#### SERVICE PERFORMANCE REPORTING

#### Consistency with Full Financial Statements and Service Performance Information

12. The information in the summary financial statements and summary service performance information shall be drawn from and be consistent with information presented in the full financial statements and service performance information for the relevant periods. Where information in the full financial statements or full service performance information for periods included in the summary financial statements or summary service performance information has subsequently been restated or reclassified, the information in the summary financial statements or summary service performance information shall be drawn from, and be consistent with, that restated or reclassified information. No further restatement or reclassification is permitted.
16. Except as otherwise required by legislation, if the entity presenting the summary financial statements and summary service performance information is an economic entity a group, the summary financial statements shall be presented for the entire economic entity group. Controlling entity financial information is not required.

#### Effective Date

...

- 44.4 PBE FRS XX *Service Performance Reporting*, issued in [Date], amended paragraphs 9, 11A, 11B, 12 and 16. An entity shall apply those amendments when it applies PBE FRS XX.

Paragraphs BC2–BC4 are added. New text is underlined.

#### Service Performance Reporting

- BC2. PBE FRS XX *Service Performance Reporting*, issued in [Date], established requirements for public benefit entities to report service performance information. At that time the NZASB made some minor amendments to PBE FRS 43 *Summary Financial Statements* to refer to both summary financial statements and summary service performance information.
- BC3. The NZASB agreed that if the full financial report included service performance information, summary financial statements should be accompanied by a summary of that service performance information. This was on the grounds that the summary should be a complete summary of the financial report. This differed from the NZASB's views on interim financial reporting where the NZASB acknowledged that there may be circumstances in which it is appropriate for an entity to produce interim financial statements but not necessarily interim service performance information.
- BC4. The NZASB also considered whether the title of PBE FRS 43 should be changed to *Summary Financial Reports* to signal that the Standard contains requirements for both financial statements and service performance information. The NZASB decided not to change the title of PBE FRS 43 at this time as it did not anticipate that the [2017] amendments would change current practice regarding when summary service performance information is presented with summary financial statements. The NZASB noted that any change in title could be considered at a later time, possibly in the context of a general amending standard.

#### XRB A1 *Application of the Accounting Standards Framework*

Paragraph 79 is added. New text is underlined.

#### D. EFFECTIVE DATE

- 79 PBE FRS XX *Service Performance Reporting*, issued in [Date], amended Appendix C. An entity shall apply that amendment when it applies PBE FRS XX.

## SERVICE PERFORMANCE REPORTING

**APPENDIX C****TIER 1 PBE ACCOUNTING REQUIREMENTS AND TIER 2 PBE ACCOUNTING REQUIREMENTS TO BE APPLIED BY PUBLIC BENEFIT ENTITIES**

*This appendix forms an integral part of XRB A1 Application of the Accounting Standards Framework.*

This appendix lists the Accounting Standards and Authoritative Notice that contain the Tier 1 PBE Accounting Requirements for Tier 1 PBEs and the Tier 2 PBE Accounting Requirements for Tier 2 PBEs.

**Accounting Standards**

PBE FRS 47 *First-time Adoption of PBE Standards by Entities Other Than Those Previously Applying NZ IFRS*

PBE FRS XX *Service Performance Reporting*

## SERVICE PERFORMANCE REPORTING

**Basis for Conclusions**

*This Basis for Conclusions accompanies, but is not part of, [draft] PBE FRS XX Service Performance Reporting.*

**Introduction**

- BC1. This Basis for Conclusions summarises the NZASB's considerations in developing PBE FRS XX *Service Performance Reporting*. Individual Board members gave greater weight to some factors than to others.
- BC2. The NZASB issued ED NZASB 2016-6 *Service Performance Reporting* in February 2016. The NZASB received 18 comment letters and obtained additional feedback through outreach on the ED. Respondents were supportive of the project but highlighted that further work was required to develop a standard that could be applied by a range of public benefit entities (PBEs).
- BC3. The NZASB revised the proposals to develop a standard that could be more readily applied by entities using a range of performance frameworks. The NZASB sought feedback on aspects of the revised proposals in [Date] 2017. It did this by notifying the respondents to the ED of the revised proposals, making contact with key constituent groups and making a near-final draft standard available on its website for a period of two months.
- BC4. The NZASB issued PBE FRS XX in [Date] 2017.

**Reasons for Issuing this Standard**

- BC5. The NZASB issued this Standard to establish requirements for the reporting of service performance information in [to](#) order address a gap in its PBE Standards and to better meet the information needs of users of general purpose financial reports. [\[edit, R5\]](#)
- BC6. When the NZASB first issued PBE Standards in 2013 it included non-integral guidance on service performance reporting in PBE IPSAS 1 *Presentation of Financial Statements*.<sup>2</sup> This non-integral guidance was based on Technical Practice Aid 9 *Service Performance Reporting* (as issued by the New Zealand Institute of Chartered Accountants in 2007) and was originally developed for application by public sector entities only. The material from TPA-9 was updated to take account of more recent developments in service performance reporting and modified to be appropriate for application by both public sector and not-for-profit (NFP) PBEs. The NZASB regarded the guidance in PBE IPSAS 1 as an interim step, pending the development of a financial reporting standard on service performance information, and subsequently added a project on service performance reporting to its agenda. This Standard is the result of that project.
- BC7. The NZASB considered the information needs of users of general purpose financial reports, as discussed in the *Public Benefits Entities' Conceptual Framework* (PBE Conceptual Framework). The NZASB noted that financial statements provide some, but not all, of the information that users of general purpose financial reports of public benefit entities require for accountability and decision making. The provision of service performance information, together with financial statements, provides users with a more complete set of information. The NZASB noted that it had already established service performance reporting requirements in the Tier 3 and Tier 4 PBE Accounting Requirements.
- BC8. The recent projects of other standard-setters were considered in developing this Standard. The International Public Sector Accounting Standards Board's (IPSASB's) Recommended Practice Guideline 3 *Reporting of Service Performance Information* (RPG 3) was issued in 2015. The NZASB considered the extent to which the guidance in RPG 3 was appropriate for PBEs in New Zealand. The Australian Accounting Standards Board (AASB) issued ED 270 *Reporting Service Performance Information* in August 2015. Although jurisdictional differences meant that the projects of the NZASB and AASB were conducted as separate projects, the Boards had similar objectives and monitored each other's projects.
- BC9. The remainder of this Basis for Conclusions is organised using the section headings in the Standard.

<sup>2</sup> Subsequently renamed *Presentation of Financial Reports*.



## SERVICE PERFORMANCE REPORTING

**Scope**

- BC10. In general, the requirements in a particular PBE Standard apply to public benefit entities in both the public sector and not-for-profit sector. However, sometimes it is necessary to differentiate between the two sectors. In the case of service performance information, the NZASB needed to consider existing legislative requirements that apply in the public sector.
- BC11. Although legislative requirements have evolved over time, many public sector PBEs such as government departments, crown entities and local governments, have been subject to performance reporting requirements for a number of years. Legislation has often required both ex ante and ex post service performance information. The NZASB was of the view that entities with existing legislative requirements to report service performance information would already have much of the information required by PBE FRS XX. In order to minimise the imposition of additional compliance costs on such entities for potentially little additional benefit, the NZASB had regard to current legislative requirements when it developed this Standard.
- BC12. The NZASB considered the implications of requiring all public sector PBEs, including those without legislative requirements to report service performance information, to comply with the Standard. The NZASB noted the following.
- (a) From a legislative perspective, there has already been an assessment for some of these entities that the costs of requiring service performance information would be greater than the benefits, that such reporting would be inappropriate, or an acknowledgement that related information is made available in other ways.
  - (b) Some entities (for example, schools) that do not have a legislative requirement to report service performance information nonetheless have a legislative requirement to report non-financial information that is complementary to the financial statements. In these circumstances imposing a different set of requirements would impose additional costs, but would not necessarily provide additional benefits commensurate with those costs.
- BC13. The concerns about conflicts with legislation were limited to the public sector. The NZASB noted that some NFP PBEs already provided service performance information in their general purpose financial reports. The NZASB was of the view that the general purpose financial report of an NFP entity should tell a story about what an NFP entity does, the resources used in doing it, and how well positioned the entity is to continue doing it. Service performance reporting is an essential component of that story. The NZASB acknowledged that complying with PBE FRS XX could lead to increased costs for NFP entities as its requirements were unlikely to align perfectly with their current reporting. The NZASB opted for a high-level principles-based approach to provide sufficient flexibility for entities to 'tell their story' in a way that is meaningful for them and their users, to avoid some of the difficulties that could arise with a more prescriptive approach and to avoid imposing unnecessary costs. On balance, the NZASB considered that the benefits of improved and more comparable service performance reporting across the NFP sector would outweigh the costs of reporting in accordance with the Standard.
- BC14. The NZASB noted that PBE FRS XX would not replace the detailed one-on-one reporting that occurs between entities and funders. Rather, it would provide an opportunity for funders to consider the extent to which the information required by the Standard could meet their needs.
- BC15. Taking all of these matters into consideration, the ED proposed that:
- (a) public sector PBEs with existing legislative requirements to report service performance information comply with the proposed standard;
  - (b) public sector PBEs without existing legislative requirements to report service performance information be encouraged, but not required, to comply with the proposed standard; and
  - (c) NFP PBEs comply with the proposed standard.
- BC16. The NZASB sought feedback on the costs and benefits of these scope proposals. Although some respondents considered that the requirements for all Tier 1 and Tier 2 PBEs should be the same, the majority of respondents supported the proposals.
- BC17. Based on feedback from respondents the NZASB refined the scope requirements for public sector PBEs to more closely link the scope with legislative requirements. For example, only some legislation requires

#### SERVICE PERFORMANCE REPORTING

service performance information in accordance with GAAP and legislation may require service performance information on only some of an entity's activities. The NZASB also agreed that, in order to acknowledge the range of legislative requirements, the scope should refer to "information in respect of service performance" rather than "a statement of service performance (by whatever name called)".

BC18. PBE FRS XX establishes requirements for the reporting of service performance information in a general purpose financial report. It does not apply to service performance information prepared for groups of entities that are not a reporting entity for financial reporting purposes or for parts of an entity. Nor does it apply to service performance information presented in another context, such as a standalone report. The NZASB considered that establishing requirements for such varied forms of reporting would not only be difficult, but would be outside its mandate. The NZASB also acknowledged that PBEs may include other types of non-financial information such as environmental information and sustainability information in an annual report, but considered that such reporting was broader than service performance reporting.

### Principles

BC19. PBE FRS XX is based on the objectives of financial reporting and the qualitative characteristics of financial reporting in the PBE Conceptual Framework.

BC20. The ED proposed that service performance information satisfy, to the extent possible, the qualitative characteristics and appropriately balance the pervasive constraints on information in general purpose financial reports. The ED explained that this should result in service performance information that is appropriate and meaningful. The NZASB introduced the term 'appropriate and meaningful' because it wanted to establish a general term that entities could apply when making judgements about the application of the qualitative characteristics and constraints. The NZASB considered that a general term such as this could facilitate discussions between preparers, and between preparers and auditors regarding the appropriate selection of information and the overall volume of information presented. The NZASB received positive feedback about the use of this term and retained it in the Standard.

BC21. In response to feedback received the NZASB:

- (a) clarified that the term appropriate and meaningful should be considered from the user's point of view;
- (b) included a discussion, from the PBE Conceptual Framework, on the trade-off needed between the qualitative characteristics; and
- (c) emphasised the role of neutrality in faithful representation.

### Information to be Reported

BC22. The NZASB's aim was to develop a standard that could be applied by a wide range of PBEs in reporting on their service performance. The ED aimed to establish best practice requirements, while acknowledging the difficulties that some entities might face in meeting the proposed requirements.

BC23. The requirements in the ED were based on the following three dimensions of service performance.

- (a) What did the entity do?
- (b) Why did the entity do it?
- (c) What impact did the entity have?

BC24. These dimensions were described using the terms outputs, outcomes and impacts. The ED defined outcomes as the impacts on society or segments of society as a result of the entity's outputs and operations. The ED proposed that all entities explain the outcomes that they seek to influence, how they consider their outputs contribute to those outcomes, and, where appropriate, what impacts the entity had on those outcomes. The ED acknowledged a number of factors that could make it difficult for some entities to report on impacts and suggested that reporting on what it referred to as intermediate outcomes could partly address these difficulties.

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BC25. Although respondents supported the development of a standard on service performance reporting, the proposed requirements were regarded as too prescriptive and too difficult for a range of entities to apply. Comments from respondents centred around the following issues.

- (a) Entities may be subject to a range of other service performance reporting requirements, including legislative requirements. Entities should be able to comply with both the proposed standard and those other requirements without restating or duplicating information.
- (b) Legislative requirements continue to evolve. For example, the terms outputs and outcomes had recently been removed from some legislation.
- (c) Differing views about whether the term impacts should be used to describe what an entity is seeking to influence or ultimate outcomes. Not-for-profit entities and public sector entities indicated that they used the term impact in differing ways.
- (d) The difficulty of attributing changes to an entity's actions, particularly when a number of entities have been working together.
- (e) A lack of clarity about when an entity was required to report on impacts.

BC26. A number of respondents suggested changes to the proposals based on the performance frameworks which they were familiar with. These suggestions highlighted that there are a number of performance frameworks being used by PBEs. Common suggestions were to generalise language, use fewer defined terms and develop higher-level requirements.

BC27. The NZASB noted this feedback and agreed that in order to achieve its objective of developing a standard that could be applied by a wide range of entities it needed to focus on high-level principles and express the requirements regarding the information to be reported in more general terms. The NZASB focused on identifying requirements that would provide useful information but which could be applied by any Tier 1 or Tier 2 PBE. This led the NZASB to require that an entity provide users with:

- (a) sufficient contextual information to understand why the entity exists, what it intends to achieve in broad terms over the medium to long term, and how it goes about this; and
- (b) information about what the entity has done during the reporting period in working towards its broader aims and objectives, as described in (a).

BC28. The Standard requires that, except as otherwise required by legislation, an entity shall present service performance information for the same reporting entity and reporting period as the financial statements. The NZASB added the reference to legislative requirements following comments from respondents that an entity may be subject to legislative requirements which specify the activities for which service performance information is required.

## Presentation

BC29. PBE FRS XX provides examples of presentation formats but does not prescribe the format of service performance information. After considering respondents' feedback on the ED the NZASB:

- (a) added a requirement that an entity clearly identify the service performance information presented in accordance with the Standard. This was in response to feedback that external parties, such as auditors, must be able to clearly identify the information that an entity has presented in order to meet the requirements of the standard; and
- (b) noted that an entity may find it helpful to present the information required by the Standard as answers to questions such as Who are we?, Why do we exist?, What did we do? and How did we perform? In the ED these questions were used to organise the information required in relation to the three dimensions of service performance. Although PBE FRS XX no longer refers to three dimensions of performance, the NZASB considered that such questions could still be a useful way of organising information.

## Comparative Information and Consistency of Reporting

BC30. The ED required prior period comparative information for all amounts reported in the service performance information and for narrative and descriptive information when it is relevant to an understanding of the current period's service performance information. The ED also noted that

## SERVICE PERFORMANCE REPORTING

PBE IPSAS 1 (together with the proposed consequential amendments) required comparisons against prospective service performance information in some circumstances.

- BC31. These proposals reflected the NZASB's view that although the most meaningful comparison of an entity's service performance is whether it achieved what it set out to achieve (being actual versus prospective comparisons), it was not appropriate to require all PBEs to provide such comparisons. Public sector PBEs are often required to publicly report on planned activities and objectives but NFP PBEs are not. The proposals in the ED reflected this difference.
- BC32. Respondents commented on the difficulty of providing comparatives for narrative information. PBE FRS XX acknowledges that judgement is required in deciding when to provide comparative narrative and descriptive information and requires that an entity considers whether such judgements should be disclosed.

### Disclosure of Judgements

- BC33. PBE FRS XX requires that an entity disclose the critical judgements made in reporting service performance information in accordance with this Standard that are relevant to an understanding of the entity's service performance information. This requirement was not in the ED, which proposed a more prescriptive approach to the information to be reported. In finalising the Standard the NZASB agreed that the Standard should be more principles-based and, therefore entities should have a high level of discretion in selecting service performance information to be reported. As a consequence of changes to be less prescriptive around the information to be reported, and thereby provide more flexibility for entities to make judgements about how best to 'tell their story', the disclosure requirements provide a necessary counterbalance, so users can understand how those judgements were made.
- BC34. The Standard sets out factors to be considered in deciding if an entity is required to disclose critical judgements in accordance with the Standard. The NZASB considered that this approach was more appropriate than mandating the disclosure of judgements by all entities.

### Effective Date

- BC35. The ED proposed a two-year implementation period. Although the majority of respondents supported a two year implementation period, others requested that the NZASB consider a longer period. Those who favoured a longer period were of the view that those responsible for governance in not-for-profit entities would need time to understand the requirements and to embed service performance reporting into their planning and management processes. They also noted the time needed to develop systems to record service performance measures and the need to implement and test systems.
- BC36. The NZASB agreed that the Standard should have a three-year implementation period, with early adoption permitted.

### Reduced Disclosure Regime Concessions

- BC37. There are no reduced disclosure regime concessions in PBE FRS XX. Because the Standard establishes high-level requirements the NZASB did not consider that it was appropriate to provide any reduced disclosure regime concessions.

### Amendments to PBE IPSAS 1

- BC38. Consistent with its view that service performance information is an integral component of a general purpose financial report, the NZASB changed the title of PBE IPSAS 1 *Presentation of Financial Statements* to *Presentation of Financial Reports* and amended PBE IPSAS 1 to refer to both financial and service performance information where appropriate. The NZASB noted that this was a significant change to PBE IPSAS 1, but considered that the changes were consistent with the PBE Conceptual Framework and would make it easier for entities preparing service performance information to understand how PBE IPSAS 1 applies to service performance information. The NZASB also noted that this approach would allow for an audit opinion on the entire general purpose financial report.
- BC39. The NZASB considered and rejected an alternative approach of making minimal changes to PBE IPSAS 1. This alternative approach would have left open the possibility of the NZASB making

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further changes to PBE IPSAS 1 at a later stage. The NZASB was of the view that this approach would have led to less clarity about the application of PBE IPSAS 1 to service performance information.

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**Tables of Concordance**

There are two tables of concordance:

- Table of Concordance: ED NZASB 2016-6; and
- Table of Concordance: Amendments to Other Standards.

These tables are provided to assist readers in identifying the changes to the proposals in ED NZASB 2016-6. The tables will not form part of a final standard.

**Table of Concordance: ED NZASB 2016-6**

This table shows how the contents of the draft standard and ED NZASB 2016-6 correspond. Paragraphs are treated as corresponding if they broadly address the same matter, even though the guidance may differ.

Changes made throughout the draft standard include the following.

- References to the three dimensions of service performance information have been omitted. The three dimensions referred to in the ED were What did the entity do?, Why did the entity do it?, and What impact did the entity have? These questions are now referred to in the presentation section as possible headings for grouping information.
- References to outputs, outcomes and impacts have been removed from requirements.
- References to performance indicators have been replaced by performance measures and/or descriptions.

Draft standard	ED	Comment
<b>Introduction</b>		
IN1-IN7	–	Includes a brief discussion of accountability and decision making. There was a longer discussion in the ED. Identifies the main features of the standard.
<b>Objective</b>		
1	1	
2	–	Added a description of service performance information.
<b>Scope</b>		
3	21	Scope requirements for not-for-profit entities and public sector entities are now separately outlined in (a) and (b). Part (b) refers to legislative requirements to provide service performance information rather than statement of service performance. Part (b) acknowledges that legislation may specify that service performance information be provided in respect of only some activities.
4	23	
5	22	
<b>Definitions</b>		
	24	The definitions section (ED paragraph 24) has been deleted. The ED defined inputs, outcomes, outputs and performance indicators and referred to impacts. Feedback from respondents demonstrated that terms are used in differing ways by different types of entities, the language used in the ED was not consistent with some outcome frameworks and the terminology differs from that used in some legislation. The NZASB therefore decided to refer to aspects of service performance in more general terms and omit the definitions.
<b>Principles</b>		
6	25	Highlights that service performance information shall be presented in the same general purpose financial report as the financial statements.
7	26	Establishes a requirement for an entity to apply the qualitative characteristics and the pervasive constraints. The ED referred to satisfying the qualitative characteristics to the extent possible. Links the phrase ‘appropriate and meaningful’ with the users of general

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Draft standard	ED	Comment
		purpose financial reports.
8	27	Expanded discussion of the qualitative characteristics in the PBE Conceptual Framework and the need to balance them.
9	28	The discussion of faithful representation now emphasises neutrality.
10	29	The draft standard notes that the pervasive constraints are identified in the PBE Conceptual Framework.
<b>Information to be Reported</b>		
11	30	Begins with the words “Except as otherwise required by legislation...”.
12	11	Shorter than paragraph 11 of the ED.
13	31	Acknowledges that there may be specific legislative requirements.
14	32	Acknowledges that some entities will be working towards long-term goals and have activities that span a number of reporting periods.
15–20	–	<p>In response to comments from constituents this section has been rewritten, drawing on a number of paragraphs in the ED.</p> <p>The ED linked information to be reported with specific questions/dimensions. The draft standard now requires contextual information and information about the current reporting period. Respondents to the ED highlighted the need for users to have sufficient contextual information to understand the environment the entity operates in.</p> <p>Paragraph 17 responds to feedback that entities should be required to explain and illustrate their intervention logic or performance frameworks.</p> <p>Paragraph 19 includes factors an entity shall consider in deciding what to report.</p> <p>Paragraph 20 is based upon paragraph 46 of the ED.</p> <p>(a) Now includes an additional example about rating scales.</p> <p>(b) Now includes high, medium, low ratings.</p> <p>(c) Now includes a reference to case studies.</p>
21	–	Based, in part, on ED paragraph 48.
22	47	
23	50	<p>No longer refers to outputs.</p> <p>Acknowledges that there may be situations in which an entity wants to mention internal activities, processes, plans or policies.</p>
24	51	
25	–	Acknowledges users’ interest in broad or longer-term effects of a project or an entity’s work.
26	–	Acknowledges the importance of comparisons and identifies a range of possible comparisons.
27	36	Terminology changes.
28	37–39	
<b>Presentation</b>		
29	–	Requires that an entity clearly identify the service performance information presented in accordance with the Standard.
30	–	Based, in part, on ED paragraph 10. The questions are identified as a possible way of presenting information rather than as dimensions of performance. The questions do not use the terms outcomes and impacts.
31	52	Replaced pie charts with infographics, added references to tables and narrative information and deleted a reference to columns.
32	53	
33	54	<p>Incorporation of information by cross-referencing was previously a sub-point. It is now located in the introductory sentences. The reference to a service performance section of a general purpose financial report has been omitted. This is because there is now a requirement (see paragraph 29 above) to clearly</p>

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Draft standard	ED	Comment
		identify the service performance information presented in accordance with the draft standard
34	55	
35	56	
<b>Comparative Information and Consistency of Reporting</b>		
36	–	This is an introductory paragraph explaining the importance of comparative information.
37	57	The requirements for ex ante performance reporting are addressed in the proposed amendments to PBE FRS 42 and PBE IPSAS 1. Now has parts (a) and (b). Refers to planned performance.
38	57	Clarified that comparatives shall be included when an amount is reported in the current period. Acknowledge judgement is required in deciding when to provide comparative narrative and descriptive information.
39	58, 59	
40	61	
41	62	Terminology changes.
42	63	
43	64	
<b>Disclosure of Judgements</b>		
44-46	–	New section. Following consideration of comments from respondents the NZASB agreed to adopt a high-level approach in drafting requirements for information to be reported. Given the increased flexibility in reporting service performance information, the NZASB agreed that users need to understand the entity's rationale for the selection of information and the judgements made by the entity in deciding what to report.
<b>Effective Date</b>		
47	65	The NZASB is now proposing a three-year implementation period. Refer BC 36.

## Table of Concordance: Amendments to Other Standards

Draft standard	ED	Comment
<b>Generic amendments</b>		The table of generic amendments changes the title of PBE IPSAS 1 in a number of standards. Most of these amendments relate to footnotes added to standards by <i>2016 Omnibus Amendments to PBE Standards</i> .
<b>PBE IPSAS 1 <i>Presentation of Financial Reports Statements</i></b>		
1	1	
2	2	
3	3	
7	7	
–	7.1	The ED proposed to delete the definition of inputs and amend the definition of outputs and outcomes. The draft standard proposes to delete the entire paragraph.
15	15	
16	16	
17	17	Paragraph 17(h) added. Paragraph 17.1 of the ED has been omitted. Paragraph 17.1 referred to outputs and outcomes. The draft standard no longer establishes requirements using the terms outputs and outcomes.



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Draft standard	ED	Comment
18	18	
19	19	
20.1	20.1	(b) Now refers to service performance information presented in accordance with PBE FRS XX. No longer refers to notes.
21	21	
24.1	24.1	
24.2	24.2	
25	25	
26	26	
27	27	The 2 <sup>nd</sup> sentence of the ED referred to outputs and outcomes. These terms are not used in the draft standard.
RDR27.1	RDR27.1	The 3 <sup>rd</sup> sentence of the ED referred to outputs and outcomes. These terms are not used in the draft standard.
28	28	
RDR28.1	–	References to financial statements changed to financial reports.
28.1	–	Incorporates <i>Amendments to PBE Standards</i> (issued December 2015) and shows proposed changes.
28.2	28.2	Incorporates <i>Amendments to PBE Standards</i> (issued December 2015) and shows proposed changes.
28.4	28.4	The 1 <sup>st</sup> sentence refers more generally to general purpose financial reporting and the 4 <sup>th</sup> sentence now says “and, where appropriate, service performance information.”
29	29	
31	31	
32	32	
33	33	
35	35	
36	36	
38	38	
39	39	
41	41	
42	42	
43	43	
44	44	Incorporates amendments to qualitative characteristics from <i>2016 Omnibus Amendments to PBE Standards</i> (issued January 2017).
45	45	
46A	46A	
46A.1	46A.1	The term outputs has been replaced with goods and services.
46A.2	46A.2	
47	47	
53	53	
53A	53A	Final sentence reworded to refer more generally to the requirements in PBE FRS XX.
54	54	New final sentence refers to PBE FRS XX.
–	55	
55.1	–	New paragraph which notes that PBE FRS XX permits, but does not require, changes to comparative information.
59	59	
60	60	

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Draft standard	ED	Comment
61	61	
62	62	
63	63	
64	64	
65	65	
66	66	
68	68	
69	69	
78		Replaced the reference to outputs with goods and services.
83	83	
85	85	
87	87	
116.1	116.1	
126.1	126.1	
127	127	
128	128	
129	129	
131	131	
132	132	
133	133	
134	134	
137	137	
138	138	
144	144	
148A	148A	
148C	148C	
148.1	148.1	
148.2	–	Adds a reference to service performance information.
149	149	
150	150	
154.1	–	The ED proposed to change the wording of an earlier effective date paragraph. It is not usual practice to do this.
154.9	154.5	
<b>PBE IAS 34 Interim Financial Reporting</b>		
Objective	Objective	Incorporates amendments to qualitative characteristics from <i>2016 Omnibus Amendments to PBE Standards</i> (issued January 2017). Now refers to users without distinguishing between types of users.
4	4	The definition of an interim financial report now refers to a “complete financial report” and a “condensed financial report.” The ED proposed a longer definition that referred to complete and condensed financial statements and service performance information. The definition in the ED implied that an interim financial report would always include service performance information. This was not consistent with other proposed changes.
8A.1	8A.1	
9.1	9.1	
9.2	9.2	
9.3	9.3	Replaced reference to outputs and outcomes with a reference to activities.

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Draft standard	ED	Comment
16A	16A	Incorporates <i>2015 Omnibus Amendments to PBE Standards</i> [July 2015]. These amendments specified when cross referencing is permitted.
19	19	Incorporates <i>Amendments to PBE Standards</i> (issued December 2015). These amendments gave effect to changes in the way the tier requirements are expressed.
RDR 19.1	RDR 19.1	Incorporates <i>Amendments to PBE Standards</i> (issued December 2015). These amendments gave effect to changes in the way the tier requirements are expressed.
21.1	21.1	
23	23	
24	24	
25	25	
25.1	–	
25.1A	–	To clarify that a comparison of prospective and historical interim service performance information would be required if an entity includes service performance information in its interim financial report and has previously published prospective service performance information for the period covered by the interim financial report.
25.2	–	
49.10	49.2	
<b>PBE FRS 42 Prospective Financial Statements</b>		
Introduction	Introduction	Incorporates amendments to qualitative characteristics from <i>2016 Omnibus Amendments to PBE Standards</i> (issued January 2017).
1	1	
3	3	
6	6	
7	7	
8	8	
9	9	The 3 <sup>rd</sup> sentence of the ED referred to outputs or outcomes. These terms are not used in the draft standard.
10	10	
11.1	11.1	
12	12	Added commas.
13	13	
14	14	
15	15	
16	16	Incorporates <i>2016 Omnibus Amendments to PBE Standards</i> (issued January 2017) which changed the qualitative characteristic and added a reference to the <i>Public Benefit Entities' Conceptual Framework</i> .
17	17	Incorporates <i>2016 Omnibus Amendments to PBE Standards</i> which changed the qualitative characteristics. The draft standard does not refer to outputs and outcomes. Changed the term performance indicators to performance measures and/or descriptions. 17(e) revised to acknowledge that aspects of service performance reporting may change over time.
18	18	
19	19	
21	21	
22	22	

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Draft standard	ED	Comment
23	23	
25	25	
26	26	Shortened subheading. The ED subheading was <i>Presentation of Prospective Financial Statements and Prospective Financial Information</i> . Added a separate sentence to deal with prospective service performance information.
27	27	
27A	27A	Rewritten. The ED referred to outputs, outcomes and impacts. The new paragraph 27A brings together the proposals in PBE FRS XX, paragraph 11A of PBE FRS 43 <i>Summary Financial Statements</i> and paragraph 41 of PBE FRS 42.
27B	–	Acknowledges that changes in information can occur over time.
41	41	
42	42	Added the 2 <sup>nd</sup> sentence (rather than amending the 1 <sup>st</sup> sentence). The final sentence now refers more consistently to “statements and information.”
43	43	
44	44	
45	45	
46	46	
47	47	Changed references to “financial statements and service performance information” to “financial reports.”
48	48	Changed references to “financial statements and service performance information” to “financial reports.”
49	49	
50	50	
51	–	
52		Removed references to outputs and outcomes.
53		
54		
55		
56		
58		
59		
60		
61		
62		
63		
64		
64.1		
65		
66		
67		
68		
69		
70.1		
73.3	73.2	
BC5	BC5	
BC6		

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<b>PBE FRS 43 <i>Summary Financial Statements</i></b>		
9	9	
11A	11A	
12	12	Corrected a reference to full service performance information to summary service performance information.
16	16	Added the introductory clause “except as otherwise required by legislation” to align with scope of PBE FRS XX.
44.4	45	
BC2–BC4	BC2–BC3	
<b>XRB A1 <i>Application of the Accounting Standards Framework</i></b>		
78	–	Added an effective date paragraph for the amendments.



NZ ACCOUNTING  
STANDARDS  
BOARD

## Memorandum

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**Date:** 1 September 2017

**To:** NZASB Members

**From:** Aimy Luu Huynh and Joanne Scott

**Subject:** **Exposure Draft PBE IPSAS 40 *PBE Combinations***

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### Action required<sup>1</sup>

1. The Board is asked to:
  - (a) PROVIDE FEEDBACK on some of the proposed modifications to IPSAS 40 *Public Sector Combinations* in developing Exposure Draft PBE IPSAS 40 *PBE Combinations* (the ED);
  - (b) NOTE the status of issues that will be considered at a future meeting; and
  - (c) NOTE the next steps of the project.

### Background

2. The objective of this project is to develop a PBE Standard based on IPSAS 40, called PBE IPSAS 40 *PBE Combinations*. IPSAS 40 deals with both acquisitions and amalgamations. The current PBE Standard dealing with combinations is PBE IFRS 3 *Business Combinations* which deals solely with acquisitions. The parts of IPSAS 40 that deal with acquisitions are based on IFRS 3 (and therefore similar to PBE IFRS 3), but, as the IPSASB did not regard this as a convergence project, there are also some differences.
3. The Board has been working through a number of issues in developing this ED. There is a range of issues. Some relate to differences between IPSAS 40 and IFRS 3 – considering why the IPSASB has diverged and whether such divergences would cause any problems for New Zealand public benefit entities (PBEs). Some relate to the distinction between amalgamations and acquisitions –whether it is clear enough and would lead to sensible answers in New Zealand. Some relate to requirements which might be open to interpretation or could be clarified.
4. The Board has already had a few sessions where it has considered differences between IPSAS 40 and PBE IFRS 3 and identified issues that it would like staff to work through. At the June 2017 NZASB meeting, the Board agreed to have a Sub-board to assist staff to progress this project and provide feedback during the development of the ED.

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<sup>1</sup> This memo refers to the work of the International Accounting Standards Board (IASB) and uses registered trademarks of the IFRS Foundation (for example, IFRS® Standards, IFRIC® Interpretations and IASB® papers).

5. This memo:
  - (a) seeks feedback on how we have actioned some of the Board's decisions in June;
  - (b) seeks feedback on new matters identified since the June meeting; and
  - (c) provides an update on the status of other issues that will be considered at a future meeting (see the appendix to this memo).<sup>2</sup>
6. The Sub-board met on 25 August 2017. This memo includes feedback from the Sub-board. As a result of that feedback some issues have come back to the Board and staff have agreed to do more work on other issues.
7. The issues in this memo vary. Some are fundamental issues because they affect the rest of the standard, or they need to be finalised before we can address other issues. Other issues are less important but, if we can get agreement on them now, then we can put them to one side and focus on the remaining issues. To assist the Board in working through the issues in this memo we have grouped the issues as high, medium or low.
8. The issues in this memo, by category, are:

High	Indicator in paragraph 12(c)
High	Voluntary combination not under common control
Medium	Tax forgiven
Medium	RDR for acquisitions
Medium	Benefits obtained by mutual agreement: (paragraph AG24)
Low	Examples of the components of an operation
Low	Identifying the acquirer
Low	Additional matters to be considered re indicators: (paragraphs AG44 and AG45)
Low	Illustrative examples

9. Attached as agenda item 7.2 is a draft marked-up copy of the ED. We have cross-referenced the issues from the memo in the ED.

**High: Indicator in paragraph 12(c)**

10. IPSAS 40 (paragraphs 12 to 14) sets out indicators that may provide evidence that the combination is an amalgamation (rather than an acquisition). At previous meetings the Board disagreed with the indicator in paragraph 12(c) because the Board was of the view that the absence of consideration does not in itself provide evidence the PBE combination is an amalgamation. The Board noted that a donated operation could be an acquisition, as illustrated in the scenario 11 example (IE121–IE129).

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<sup>2</sup> We are not seeking feedback on the issues in the appendix. It has been provided to give an overview of all the issues being considered in this project and to provide a status report on work in progress.

11. The Board also disagreed with the classification of the combination in scenario 6 (IE63–IE71) as an amalgamation, on the grounds that it has a similar fact pattern to scenario 11. The major difference between the two scenarios is that in scenario 6 the whole entity is transferred, whereas in scenario 11 only part of an entity is transferred in. The Board did not think that this difference between the two scenarios was sufficient grounds for a different classification decision.
12. At the June 2017 meeting the Board agreed to remove the indicator in paragraph 12(c) (shown below).
  12. The following indicators may provide evidence that the combination is an amalgamation:
    - (a) Consideration is paid for reasons other than to compensate those with an entitlement to the net assets of a transferred operation for giving up that entitlement (paragraphs AG27–AG28 provide additional guidance);
    - (b) Consideration is not paid to those with an entitlement to the net assets of a transferred operation (paragraphs AG29–AG30 provide additional guidance); or
    - (c) Consideration is not paid because there is no-one (whether an individual or an entity) with an entitlement to the net assets of a transferred entity (paragraph AG31 provides additional guidance).
13. The Board felt that the removal of this indicator would also be consistent with the broader view of the definition of equity interests and owners in New Zealand. In the New Zealand public sector and not-for-profit (NFP) sector, the concept of equity interests is not limited to equity participants in an equity instrument and use of the term owners is not limited to owners with a quantifiable ownership interest.
14. At the June meeting the Board also suggested that the ED would require further work to give effect to the removal of the indicator in paragraph 12(c). The Board requested that staff:
  - (a) strengthen the conclusions in the illustrative examples that had previously relied on this indicator;
  - (b) explain more clearly why scenario 6 in the illustrative examples should be classified as an acquisition; and
  - (c) draft an explanation for the Basis for Conclusions as to why we removed this indicator.
15. Staff made these changes and sought feedback from the Sub-board on the drafting changes to give effect to the removal of this indicator in 12(c) and the change in the classification in scenario 6 from an amalgamation to an acquisition. On reflection, the Sub-board thought there was insufficient guidance in paragraph 12(a) and (b) (as per IPSAS 40) to indicate that the combination should be classified as an acquisition. The Sub-board noted that paragraph 12(b) has a bracketed reference to paragraphs AG29–AG30 which explain that when there has been no consideration an entity needs to consider why, but the messages in AG29–AG30 are not evident from a simple cross reference. The Sub-board suggested expanding paragraph 12(b) to remind entities to consider why no consideration was paid.



16. We have made these changes (see below), drafted the supporting Basis for Conclusions (BC3–BC6) and are now seeking feedback on whether these changes have addressed the Board’s concerns.
12. The following indicators may provide evidence that the combination is an amalgamation:
- (a) Consideration is paid for reasons other than to compensate those with an entitlement to the net assets of a transferred operation for giving up that entitlement (paragraphs AG27–AG28 provide additional guidance); or
  - (b) Consideration is not paid to those with an entitlement to the net assets of a transferred operation. However, an entity is still required to consider the reasons why no consideration is paid (paragraphs AG29–AG30 provide additional guidance).; ~~or~~
  - (c) [Not used] ~~Consideration is not paid because there is no one (whether an individual or an entity) with an entitlement to the net assets of a transferred entity (paragraph AG31 provides additional guidance).~~
17. We would like to check that the Board agrees with all of the changes made to give effect to the removal of the indicator in 12(c) and the changes to scenarios.

#### Questions for the Board

Q1. Does the Board agree with the proposed changes to the following paragraphs?

- paragraph 12(b)
- scenario 2, variation (paragraphs IE20–IE22)
- scenario 3 (paragraphs IE30–IE32)
- scenario 6 (paragraphs IE69–IE71)
- scenario 14 (paragraphs IE154 and IE156)

Q2. Does the Board agree with the draft Basis for Conclusions in BC3–BC6?

#### High: Voluntary combination not under common control

18. IPSAS 40 does not provide guidance for voluntary combinations not under common control. The Board felt that it was important that the ED provide guidance for such combinations as they do occur in the NFP sector in New Zealand.
19. We therefore developed the guidance in paragraph AG38.1 and an illustrative example, scenario 15 (IE156.1–IE156.8).
20. At the June 2017 meeting, the Board agreed with the inclusion of paragraph AG38.1 but requested that staff replace scenario 15 with a clearer and simpler example.
21. We have updated the illustrative example, scenario 15 in paragraphs IE156.1–IE156.8.

#### Question for the Board

Q3. Does the Board agree with the proposed illustrative example, scenario 15 in paragraphs IE156.1–IE156.8?

## Medium: Tax forgiven

22. Following a query by a Board member about the intention of the guidance in IPSAS 40 on tax forgiven (see paragraphs 33, 78, AG57 and AG86 shown below), we reviewed all the guidance on tax forgiven. We could understand the concern and wondered whether some of the paragraphs were necessary as, in some cases, they merely seemed to be reminding entities to look at the requirements in other standards. We are proposing to keep some of the guidance and to delete some (as shown below). Our reasons are also explained below.
33. Amalgamations involving PBE entities may result in a tax authority forgiving amounts of tax due as part of the terms of the amalgamation. The resulting entity shall not recognise any taxation items that are forgiven as a result of the terms of the amalgamation (paragraphs AG57–AG58 provide related application guidance).
34. ~~[Not used] The resulting entity shall recognize and measure any remaining taxation items included in or arising from an amalgamation in accordance with the relevant international or national accounting standard dealing with income taxes. The resulting entity shall recognize and measure any remaining revenue from taxation included in or arising from an amalgamation in accordance with IPSAS 23, *Revenue from Non-Exchange Transactions (Taxes and Transfers)*.~~
- ...
78. Acquisitions by a PBE entity may result in a tax authority forgiving amounts of tax due as part of the terms of the acquisition. The acquirer shall not recognise any taxation items that are forgiven as a result of the terms of the acquisition (paragraphs AG85 ~~and~~ – AG87 provide related application guidance).
79. ~~[Not used] The acquirer shall recognize and measure any remaining taxation items included in or arising from an acquisition in accordance with the relevant international or national accounting standard dealing with income taxes. The acquirer entity shall recognize and measure any remaining revenue from taxation included in or arising from an acquisition in accordance with IPSAS 23.~~
- ...
- AG57. The resulting entity shall not recognise any amounts in respect of a combining operation's tax due where these amounts have been forgiven by a tax authority as part of the terms of the amalgamation. Where tax forgiveness occurs subsequent to an amalgamation, the resulting entity applies the requirements in paragraph 49. In applying the modified pooling of interests method of accounting, the resulting entity shall treat those amounts included in the terms of the amalgamation as having been derecognised prior to the amalgamation. The resulting entity shall account for a combining operation's tax due that has not been forgiven by a tax authority in accordance with PBE IAS 12.
- AG58. ~~[Not used] Where, as a result of the amalgamation, the resulting entity becomes the tax authority, it shall derecognize any tax receivable relating to the combining operation's tax due that has been forgiven in accordance with IPSAS 23, *Revenue from Non-Exchange Transactions (Taxes and Transfers)*.~~
- AG86. ~~[Not used] If the acquirer is itself the tax authority, it shall derecognize any tax receivable relating to the acquired operation's tax due that has been forgiven in accordance with IPSAS 23.~~
23. These paragraphs refer to situations where the tax authority is the resulting entity. The remaining revenue refers to the tax authority's tax receivable with external parties after the inter-entity eliminations and combining operations' tax forgiven. The remaining revenue (with external entities) is accounted for under IPSAS 23.
24. We have checked why some of this guidance was included in IPSAS 40. One possibility is that it might have been included because some entities applying IPSASs might not have otherwise eliminated such balances.

25. We propose to delete paragraphs 34, 79, AG58 and AG86 on the grounds that they could create confusion and there is sufficient guidance on tax forgiven as part of the combination in the remaining paragraphs.
26. We also propose to change paragraphs IE176 and IE250 which refer to tax forgiven as shown below. These changes are proposed to clarify that any *remaining* tax receivable is accounted for in accordance with PBE IPSAS 23 and to make the tax forgiven the first idea in the sentences.  
  
IE176. MF would recognise an adjustment for the tax forgiven, and would account for the remaining tax receivable in accordance with PBE IPSAS 23, ~~and would recognise an adjustment for the tax forgiven.~~  
  
IE250. MF would recognise an adjustment for the tax forgiven, and would account for the remaining tax receivable in accordance with PBE IPSAS 23, ~~and would recognise an adjustment for the tax forgiven.~~
27. We also propose adding the income tax guidance from PBE IFRS 3.24 as paragraph 79.1.

79.1 The acquirer shall recognise and measure a deferred tax asset or liability arising from the assets acquired and liabilities assumed in a PBE combination in accordance with PBE IAS 12.

#### Questions for the Board

- Q4. Does the Board agree with the recommendation to:  
  - (a) delete paragraphs 34, 79, AG58 and AG86; and
  - (b) change the order of wording in paragraphs IE176 and IE250?
- Q5. Does the Board agree to add income tax guidance from PBE IFRS 3.24 as paragraph 79.1?

#### Medium: RDR for acquisitions

28. We have aligned the RDR concessions and RDR paragraphs for acquisition disclosures with the proposals for NZ IFRS 3 *Business Combinations* in ED NZASB 2017-1 *Amendments to RDR for Tier 2 For-profit Entities*.
29. We have also applied the *Draft Policy for Determining RDR for Tier 2 Entities in Australia and Tier 2 Entities For-Profit Entities in New Zealand* to the IPSAS-specific acquisition disclosures in IPSAS 40. We will consider the RDR concessions for the amalgamation disclosures at a future meeting.

#### Question for the Board

- Q6. Does the Board agree with the proposed RDR concessions and RDR paragraphs for acquisition disclosures in paragraphs 119–RDR 125.1?

#### Medium: Benefits obtained by mutual agreement (para AG24)

30. In June 2017 some Board members commented that they found paragraph AG24 (see below) confusing. The Board asked staff to discuss the purpose of paragraph AG24 with IPSASB staff before proposing any amendments.

AG24. An acquisition is usually a mutual agreement between two or more parties, and usually has commercial substance. However, in the public sector, a party to the combination may be able to impose a public sector combination on the other party to the combination. Where this results in the entity gaining access to economic benefits or service potential that are similar to those that could have been obtained by mutual agreement, it is probable that the economic substance of the public sector combination is that of an acquisition. For example, a central government may centralize a service for which it had been providing funding, by requiring local government entities to transfer operations to the central government in order to achieve economies of scale. Where the entity does not gain access to economic benefits or service potential that are similar to those that could have been obtained in a voluntary transaction, it is probable that the economic substance of the public sector combination is that of an amalgamation.

31. We have discussed this IPSASB staff and not identified any reason why removing the discussion of the types of benefits or service potential obtained would affect the classification of transactions. We therefore propose amending paragraph AG24 as outlined below. We also propose to remove the paragraph AG24 text from paragraphs IE19, IE29, IE45 and IE59.

An acquisition is usually a mutual agreement between two or more parties, and usually has commercial substance. However, it is possible for an acquisition to occur without mutual agreement (for example, a forced nationalisation). ~~in the public sector, a party to the combination may be able to impose a public sector combination on the other party of the combination. Where this results in the entity gaining access to economic benefits or service potential that are similar to those that could have been obtained by mutual agreement, it is probable that the economic substance of the public sector combination is that of an acquisition. For example, a central government may centralize a service for which it had been providing funding, by requiring local government entities to transfer operations to the central government in order to achieve economies of scale. Where the entity does not gain access to economic benefits or service potential that are similar to those that could have been obtained in a voluntary transaction, it is probable that the economic substance of the public sector combination is that of an amalgamation.~~

#### Question for the Board

- Q7. Does the Board agree with the proposed amendments to paragraph AG24 and the consequential changes to paragraphs IE19, IE29, IE45 and IE59?

#### Low: Examples of the components of an operation

32. The application guidance in IPSAS 40 (paragraph AG4) defines the three elements of an operation (being inputs, processes and outputs). However, it does not include some of the examples of those elements that are provided in PBE IFRS 3 paragraph B7.
33. We think these examples would be useful for PBEs and propose to include them in the ED. The examples from PBE IFRS 3 are shown in table 1 below.

Table 1

IPSAS 40	PBE IFRS 3
AG4. (a) <b>Input:</b> Any economic resource that creates, or has the ability to create, outputs when one or more processes are applied to it.	B7. (a) <b>Input:</b> Any economic resource that creates, or has the ability to create, outputs when one or more processes are applied to it. Examples include non-current assets (including intangible assets or rights to use non-current assets), intellectual property, the ability to obtain access to necessary materials or rights and employees.
(b) <b>Process:</b> Any system, standard, protocol, convention or rule that when applied to an input or inputs, creates or has the ability to create outputs.	(b) <b>Process:</b> Any system, standard, protocol, convention or rule that when applied to an input or inputs, creates or has the ability to create outputs. Examples include strategic management processes, operational processes and resource management processes. These processes typically are documented, but an organised workforce having the necessary skills and experience following rules and conventions may provide the necessary processes that are capable of being applied to inputs to create outputs. (Accounting, billing, payroll and other administrative systems typically are not processes used to create outputs.)

#### Question for the Board

Q8. Does the Board agree to include the examples of inputs and processes from PBE IFRS 3 in the ED?

#### Low: Identifying the acquirer

34. Some Board members were concerned that one might not be able to identify an acquirer in a reverse acquisition. IFRS 3 (paragraph B14–B18) includes guidance on this but this guidance was omitted from IPSAS 40. The Board asked staff to check why this guidance was omitted from IPSAS 40.
35. IPSASB staff suggested that there were a few reasons for omitting this guidance. They were:
  - (a) the existence of the classification approach in IPSAS 40. IFRS 3 requires acquisition accounting so entities have to identify an acquirer;
  - (b) to avoid conflict with amalgamations. The classification approach in IPSAS 40 is if no party to a combination gains control, the combination shall be classified as an amalgamation. Whereas if one party gains control in a combination, this indicates it may be an acquisition and an acquirer has been identified; and
  - (c) the exchange of equity instruments in the public sector is not common and unlikely to occur unless there is a corporation involved.

36. We do not propose to include additional guidance on reverse acquisitions in the ED on the basis that reverse acquisitions are not common in the PBE sector. Preparers can refer to NZ IFRS 3 *Business Combinations* for authoritative guidance for identifying an acquirer in a reverse acquisition.

**Question for the Board**

- Q9. Does the Board agree not to include any additional guidance for identifying an acquirer in a reverse acquisition in the ED?

**Low: Additional matters to be considered re indicators (paragraphs AG44 and AG45)**

37. The Board has previously suggested drafting changes to paragraphs AG44 and AG45. The Board had agreed to keep the original text about user information needs in paragraph AG44 and in the table that forms part of paragraph AG45 and suggested adding “where paid” after “initial investments made”.
38. We propose amending paragraph AG44 and the table in paragraph AG45 as outlined below.

AG44. The acquisition method views a combination from the perspective of the acquirer—the entity that gains control of the other operations. The acquirer purchases or otherwise gains control over net assets and recognises in its financial statements the assets acquired and liabilities assumed, including those not previously recognised by the acquired operation. Such information assists users of the financial statements in assessing the initial investments made, where paid, and the subsequent performance of those investments and comparing them with the performance of other entities based on the investment made by the acquirer. ~~It also includes information about the market’s expectation of the value of the future cash flows associated with those assets and liabilities.~~ While it revalues the assets and liabilities of the acquired operation, it does not affect the valuation of assets and liabilities held by the acquirer prior to the acquisition. Further, depending on the relationship between the amounts in paragraph 85(a) and 85(b) and other factors (for example, a bargain purchase), it may result in the immediate recognition of a gain or loss through surplus or deficit.

...

AG45. The information provided by each approach is summarised in the following table.

	<b>Amalgamation</b>	<b>Acquisition</b>
Perspective	Perspective of each of the combining operations and their owners or constituents.	Perspective of the acquirer.
User information	Assists users of the financial statements in assessing the performance of the resulting entity based upon the combined historical assets and liabilities of the combining operations at the date of the amalgamation and in comparing operating results with prior periods.	Assists users of the financial statements in assessing the initial investments made, <u>where paid</u> , and the subsequent performance of those investments.

**Question for the Board**

Q10. Does the Board agree with the proposed amendments to paragraph AG44 and the table in paragraph AG45?

**Low: Illustrative examples**

39. Some of the illustrative examples contain the text below.

IE68. In considering the economic substance of the PBE combination, the Department of Health notes that the combination does not result in a controlling entity/controlled entity relationship between the Department and Not-for-Profit Organisation I. This is consistent with both an amalgamation and an acquisition.

40. We queried the purpose of this text in the examples because we considered that the absence of a controlling entity/controlled entity relationship would be *more* consistent with an amalgamation than an acquisition. Also, if the presence or absence of such a relationship does not help with the classification of the transaction we did not see the point of considering this point. We raised this matter with IPSASB staff and they clarified that the presence or absence of controlling entity/controlled entity relationship is not conclusive as to the type of combination. The lack of a controlling entity/controlled entity relationship is consistent with an amalgamation, but could also be consistent with an acquisition as an operation could be acquired and fully integrated into the acquirer. Therefore entities would need to consider other factors to determine the type of combination.

41. We propose deleting this text from the ED because, in our view, it does not assist an entity to classify a combination, and we think it could create confusion. The affected paragraphs are IE19, IE29, IE45 and IE68.

**Question for the Board**

Q11. Does the Board agree to delete paragraphs IE19, IE29, IE45 and IE68 in the ED?

**Next steps**

42. Table 2 below provides the tentative project timeline. We hope to issue the ED by the end of this year, but this is subject to the Sub-board and Board working through the issues and the number of changes we make. If the ED is not issued in December the proposed timing would move out by a number of months.

**Table 2**

Project milestones	Dates
Continue to develop ED	September – December 2017
Issue Invitation to Comment and ED	December 2017
Deadline for comments	End of April 2018
Consider comments and develop draft standard	May – July 2018

Project milestones	Dates
Issue PBE Standard	August 2018

### Recommendations

43. We recommend that the Board:

- (a) PROVIDES FEEDBACK on the proposed modifications to IPSAS 40 *Public Sector Combinations* in developing Exposure Draft PBE IPSAS 40 *PBE Combinations*;
- (b) NOTES the status of the other issues that will be considered at a future meeting; and
- (c) NOTES the next steps of the project.

### Attachment

Agenda item 7.2: Draft ED PBE IPSAS 40 *PBE Combinations* (marked-up)



## Appendix: Status of other issues

The table below provides a summary of the status of the other issues that will be considered at a future meeting. These issues are still work in progress and we are not seeking Board decisions at this meeting.

Level of importance	Comments to date	Status
High	<p><u>Definition of equity interests and owners</u></p> <p>At the March 2017 meeting, the Board agreed to change the definition of equity interests and owners in IPSAS 40 and to align the definitions with those in PBE IFRS 3 <i>Business Combinations</i>. The June 2017 agenda papers showed the changes proposed to the IPSAS 40 definitions (see below).</p> <p>For the purposes of this Standard, <b>equity interests</b> is used broadly to mean ownership interests of investor-owned entities and owner, member or participant interests of mutual entities. <u>In the context of this Standard equity interests may also mean ownership interests established by other mechanisms such as deed or statute.</u></p> <p>For the purposes of this Standard, <b>owners</b> is used broadly to include <del>any party with quantifiable ownership interests in an operation. This includes, but is not limited to,</del> holders of equity interests of investor-owned entities and owners or members of, or participants in, mutual entities.</p> <p>At the June 2017 meeting, a Board member thought the proposed amendments may not be sufficiently broad to cover the interests of beneficiaries in a trust. The Board asked staff to consider modifying the definitions to make sure they encompassed trusts but to maintain consistency with the <i>Public Benefit Entities' Conceptual Framework</i>.</p> <p>Post June: We looked at the PBE Conceptual Framework and noted that it says very little about ownership interests and trusts. Rather than trying to acknowledge the rights of beneficiaries in the definitions of equity interests and owners we proposed including additional comments about these terms under a separate subheading at the end of the definitions section.</p> <p>The Sub-board considered the staff's suggestions (in August) but did not support the staff's proposals. The Sub-board requested further work on the definitions to bring in the different types of PBEs and different types of residual interests in PBEs.</p>	<p>We will redraft the definitions of equity interests and owners for the Sub-board and Board consideration at a future meeting.</p>

Level of importance	Comments to date	Status
High	<p><u>Reference to new entity and resulting entity</u></p> <p>The Board had concerns with the use of the term “new entity” in paragraphs AG17 and AG22. The use of this term in paragraphs AG17 and AG22 was inconsistent/confusing – paragraph AG17 uses the term “new entity” to refer to a new legal entity but paragraph AG22 uses the term “new entity” to refer to a new economic entity.</p> <p>The IPSASB’s thinking is that an amalgamation effectively creates a new entity. The new entity could be a new legal form or new economic form i.e. continuing entity.</p> <p>We reviewed the use of the terms “new entity” and “resulting entity” in IPSAS 40. In June 2017 we proposed a number of changes (including using the words “new <u>legal</u> entity” where appropriate) to clarify what is meant.</p> <p>We have since identified the use of “legal” in these paragraphs would not work in instances where an entity is not a separate legal entity (for example, government departments and possibly some trusts).</p> <p>Clarity over the use of “new entity” is important because it affects presentation, disclosure and how to apply the modified pooling of interests method (see below).</p> <p>The Sub-board agreed that staff should continue to work on this issue, possibly by defining “new entity” and/or including an explanation of the circumstances that can give rise to new entities and continuing entities under the section <i>Identifying the Resulting Entity</i> (paragraphs 17–18).</p>	We will continue to work on this issue for the Sub-board and Board consideration at a future meeting.
High	<p><u>Modified pooling of interests method</u></p> <p>A Board member sought clarification about the paragraphs explaining how to apply the modified pooling of interests method to amalgamations. The Board member noted that there seemed to be an inconsistency between paragraph 16(c) and paragraphs 21 and 23 and queried which takes precedent.</p> <p>Paragraph 16(c) requires the recognition and measurement of assets and liabilities “consistent with the requirements in IPSASs”. Paragraph 21 requires the recognition of the assets and liabilities that were recognised by the combining operations at the amalgamation date. Paragraph 23 requires that the assets and liabilities recognised meet the definitions in the Conceptual Framework at the amalgamation date. Our understanding is that paragraph 16(c) expresses what is intended to be the over-riding requirement. The intention is the resulting entities’ accounting policies and recognised assets and liabilities should be consistent with IPSASs.</p>	We will draft the guidance for Sub-board and Board consideration at a future meeting.

Level of importance	Comments to date	Status
	<p>It is not immediately clear what IPSAS 40 would require if one of the combining entities had previously recognised assets and liabilities that did not meet the recognition and measurement requirements in IPSASs or if it had failed to recognise assets and liabilities that should be recognised in accordance with IPSASs. This led us to query the circumstances in which the resulting entity would be expected to apply IPSAS 33 <i>First-time Adoption of Accrual Basis IPSASs</i>. IPSAS 40 has not provided guidance on when the first-time adoption standard would be applied, it has been left to the judgement of the reporting entity (see BC83–BC85). There are situations where the resulting entity may need to apply the first-time adoption standard, such as when the resulting entity is a new entity and the combining entities are not already applying PBE Standards. We think it would be helpful for New Zealand constituents if we spell out what is required in different situations. The Sub-board agreed additional guidance is necessary to clarify how to apply the modified pooling of interests method to different types of amalgamations and the circumstances in which an entity would be a first time adopter.</p>	
High	<p><u>Prior period information</u></p> <p>We were asked to consider whether the requirements for prior period information are sufficiently clear and work well together. We have identified some ways in which we could clarify some of the requirements in IPSAS 40.</p> <p>The particular issue that was raised was how paragraph 50(a) interacts with paragraph 52, when an entity elects to present information for periods prior to the amalgamation date and whether the guidance in IPSAS 40 is sufficiently clear. Paragraph 50 sets out the requirements for the first set of financial statements for a resulting entity (new economic entity) following an amalgamation.</p> <p>50. ...</p> <p>(a) <b>An opening statement of financial position as of the amalgamation date;...</b></p> <p>52. Subject to the requirements in paragraphs 54 and 56, the resulting entity is permitted but not required to present financial statements for periods prior to the amalgamation date (paragraphs AG64–AG65 provide related application guidance). Where a resulting entity elects to present financial statements for periods prior to the amalgamation date, it shall disclose the information required by paragraph 54(g).</p> <p>We have considered whether the presentation and disclosure guidance for an amalgamation (in paragraphs 50–57 and AG64) is sufficiently clear. For example, we considered how easy it would</p>	<p>We will draft the updated requirements for Sub-board and Board consideration at a future meeting.</p>

Level of importance	Comments to date	Status
	<p>be for a continuing entity to identify whether it is required to present prior period comparatives. This took some time and involved going back and forth between parts of the standard to ascertain how all the requirements fit together. We have identified areas where the guidance could be clarified.</p> <p>The Sub-board agreed that staff should seek to clarify some of the presentation and disclosure requirements regarding prior period information for amalgamations.</p>	
High	<p><u>Transition</u></p> <p>The transitional guidance in IPSAS 40 (paragraphs 129–133 and AG114–AG115) came from IFRS 3 but needs to be considered in the New Zealand context. It was included in IFRS 3 to address transition issues that could have arisen for entities at that time, having regard to the accounting they applied before adoption of IFRS 3. In contrast, most PBEs will be moving from PBE IFRS 3 to PBE IPSAS 40 and would have applied PBE IFRS 3 to any recent combinations within the scope of PBE IFRS 3. Because of this we might need less (or slightly different) transitional guidance than that in IPSAS 40.</p> <p>For example, it has been suggested that IPSAS 40 paragraph AG115(e) might not work for entities that have already applied PBE IFRS 3 or other earlier standards. It is unlikely that New Zealand PBEs would have negative goodwill or goodwill deducted from equity.</p> <p>When we developed PBE IFRS 3 we removed the transitional provisions because most PBEs (mainly public sector entities) were already applying NZ IFRS 3. We also agreed not to permit retrospective application of PBE IFRS 3 on the basis that it would be costly for entities that had not previously applied NZ IFRS to adjust assets and liabilities acquired in a business combination whose acquisition date preceded the start of the comparative period on application of PBE IFRS 3.</p> <p>The Sub-Board has proposed that staff develop New Zealand specific transition provisions.</p>	<p>We will draft New Zealand specific transition provisions for Sub-board and Board consideration at a future meeting.</p>
Medium	<p><u>Guidance for selecting the accounting policies in the resulting entity</u></p> <p>We have been asked to consider how much choice a resulting entity would have in selecting its accounting policies and the interaction between IPSAS 40 and IPSAS 3 <i>Accounting Policies, Changes in Accounting Estimates and Errors</i>. We have also been asked to consider whether the requirements in IPSAS 40 about accounting policy selection are sufficiently clear. Paragraph 28 of the ED is shown below.</p> <p>28. The modified pooling of interests method results in a single combined resulting entity. A single uniform set of accounting</p>	<p>We will redraft the application guidance for Sub-board and Board consideration at a future meeting.</p>

Level of importance	Comments to date	Status
	<p>policies, consistent with the requirements of PBE Standards, is adopted by that entity, and the carrying amounts of the identifiable assets and liabilities of the combining operations are adjusted, where required, to conform to those accounting policies.</p> <p>IPSAS 3 has guidance on initial selection of policies and changes in policies. The circumstances of a combination would dictate which parts of IPSAS 3 an entity applied in selecting policies. We have confirmed with IPSASB staff that a new entity would be unable to apply the guidance in IPSAS 3 on changes in accounting policies. A continuing entity would apply the guidance in IPSAS 3 on changes in accounting policies.</p> <p>We had drafted additional application guidance on the selection of accounting policies by the resulting entity for the Sub-board's feedback.</p> <p>The Sub-board thought additional application guidance on the selection of accounting policies by the resulting entity would be helpful, but requested further work on what that guidance should say and how it should distinguish between continuing and new entities. The Sub-board considered that there should be an expectation that a continuing entity would retain its prior accounting policies.</p>	
Medium	<p><u>Deferred tax on amalgamations</u></p> <p>A Sub-board member queried if we should draft an equivalent to paragraph 79.1 (shown below) for amalgamations.</p> <p>79.1 The acquirer shall recognise and measure a deferred tax asset or liability arising from the assets acquired and liabilities assumed in a PBE combination in accordance with PBE IAS 12.</p> <p>We checked with IPSASB staff if the possibility of deferred tax arising in an amalgamation had been contemplated when IPSAS 40 was developed. IPSAS 40 did not rule out this possibility but it did not provide guidance on deferred taxes because the income tax law for combinations is different in each jurisdiction. IPSAS 40 refers entities to the international or national standard on income tax for guidance.</p>	We will consider this further and will report back to the Sub-board and Board at a future meeting.

Draft for discussion  
At this meeting we are proposing to discuss only those issues identified in agenda item 7.1.



## EXPOSURE DRAFT NZASB 2017-X

### **PUBLIC BENEFIT ENTITY INTERNATIONAL PUBLIC SECTOR ACCOUNTING STANDARD 40 PBE COMBINATIONS (PBE IPSAS 40)**

#### **Issued [Date]**

This [draft]<sup>1</sup> Standard was issued on [date] by the New Zealand Accounting Standards Board of the External Reporting Board pursuant to section 12(a) of the Financial Reporting Act 2013.

This [draft] Standard is a disallowable instrument for the purposes of the Legislation Act 2012, and pursuant to section 27(1) of the Financial Reporting Act 2013 takes effect on [date].

Reporting entities that are subject to this [draft] Standard are required to apply the [draft] Standard in accordance with the effective date set out in paragraph 126.1.

In finalising this [draft] Standard, the New Zealand Accounting Standards Board has carried out appropriate consultation in accordance with section 22(1) of the Financial Reporting Act 2013.

This [draft] New Zealand Tier 1 and Tier 2 Public Benefit Entity Accounting Standard has been issued as a result of a new International Public Sector Accounting Standard.

This [draft] Standard when applied, supersedes PBE IFRS 3 *Business Combinations*.

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<sup>1</sup> References to “this Standard” throughout this Exposure Draft should be read as referring to “this draft Standard”.

## **PBE IPSAS 40 PBE COMBINATIONS**

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ISBN

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[Appendix A: Application Guidance](#)

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Basis for Conclusions

IPSASB Basis for Conclusions<sup>2</sup>

Implementation Guidance

Illustrative Examples

Comparison with IPSAS 40

History of Amendments

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Public Benefit Entity International Public Sector Accounting Standard 40 [PBE Combinations](#) is set out in paragraphs 1–[134.1](#) and Appendices A [and B](#). All the paragraphs have equal authority. PBE IPSAS 40 should be read in the context of its objective, the NZASB’s Basis for Conclusions on PBE IPSAS 40, the IPSASB’s Basis for Conclusions on IPSAS 40, the *Public Benefit Entities’ Conceptual Framework* and Standard XRB A1 *Application of the Accounting Standards Framework*. PBE IPSAS 3 *Accounting Policies, Changes in Accounting Estimates and Errors* provides a basis for selecting and applying accounting policies in the absence of explicit guidance.

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<sup>2</sup> For the purpose of this Exposure Draft, the IPSASB’s Basis for Conclusions has been included to assist constituents. When the PBE Standard is issued, the IPSASB’s Basis for Conclusions will be available as additional material on the XRB website.

## Objective

1. The objective of this Standard is to improve the relevance, faithful representativeness and comparability of the information that a reporting entity provides in its financial statements about a ~~PBE public sector~~ combination and its effects. To accomplish that, this Standard establishes principles and requirements for how:
  - (a) A reporting entity classifies a ~~PBE public sector~~ combination as an amalgamation or an acquisition;
  - (b) A resulting entity recognises and measures in its financial statements the identifiable assets received, the liabilities assumed and any non-controlling interest in an amalgamation;
  - (c) A resulting entity recognises and measures components of net assets/equity and other adjustments recognised in an amalgamation;
  - (d) An acquirer recognises and measures in its financial statements the identifiable assets acquired, the liabilities assumed and any non-controlling interest in the acquired operation;
  - (e) An acquirer recognises and measures the goodwill acquired in, or the gain or loss arising from, an acquisition; and
  - (f) A reporting entity determines what information to disclose to enable users of the financial statements to evaluate the nature and financial effects of a ~~PBE public sector~~ combination.

## Scope

- 1.1 **This Standard applies to Tier 1 and Tier 2 public benefit entities.**
- 1.2 **A Tier 2 entity is not required to comply with the requirements in this Standard denoted with an asterisk (\*). Where a Tier 2 entity elects to apply a disclosure concession it shall comply with any RDR paragraphs associated with that concession.**
2. An entity that prepares and presents financial statements ~~under the accrual basis of accounting~~ shall apply this Standard in accounting for ~~PBE public sector~~ combinations.
3. This Standard applies to a transaction or other event that meets the definition of a ~~PBE public sector~~ combination. This Standard does not apply to:
  - (a) The accounting for the formation of a joint arrangement in the financial statements of the joint arrangement itself.
  - (b) The acquisition or receipt of an asset or a group of assets (and any related liabilities) that does not constitute an operation. In such cases an entity shall identify and recognise the individual identifiable assets acquired or received (including those assets that meet the definition of, and recognition criteria for, intangible assets in PBE IPSAS 31 *Intangible Assets*) and liabilities assumed. Such a transaction or event does not give rise to goodwill.
  - (c) The assumption of a liability or a group of liabilities that does not constitute an operation. In such cases an entity shall identify and recognise the individual liabilities assumed.
4. The requirements of this Standard do not apply to the acquisition by an investment entity, as defined in PBE IPSAS 35 *Consolidated Financial Statements*, of an investment in a controlled entity that is required to be measured at fair value through surplus or deficit.

## Definitions

5. The following terms are used in this Standard with the meanings specified:

**A PBE is a public benefit entity. A PBE is a reporting entity whose primary objective is to provide goods or services for community or social benefit and where any equity has been provided with a view to supporting that primary objective rather than for a financial return to equity holders.**

**A ~~PBE public sector~~ combination is the bringing together of separate operations into one ~~PBE public sector~~ entity.**

*General definitions related to all ~~PBE public sector~~ combinations*

For the purposes of this Standard, **equity interests** is used broadly to mean ownership interests of investor-owned entities and owner, member or participant interests of mutual entities. **In the context**

of this Standard equity interests may also mean ownership interests established by other mechanisms such as deed or statute.

An asset is identifiable if it either:

- (a) Is separable, i.e., is capable of being separated or divided from the entity and sold, transferred, licensed, rented, or exchanged, either individually or together with a related binding arrangement, identifiable asset or liability, regardless of whether the entity intends to do so; or
- (b) Arises from binding arrangements (including rights from contracts or other legal rights), regardless of whether those rights are transferable or separable from the entity or from other rights and obligations.

A mutual entity is an entity, other than an investor-owned entity, that provides dividends, lower costs or other economic benefits directly to its owners, members or participants. For example, a mutual insurance company, a credit union and a co-operative entity are all mutual entities.

An operation is an integrated set of activities and related assets and/or liabilities that is capable of being conducted and managed for the purpose of achieving an entity's objectives, by providing goods and/or services for community or social benefit, rather than a financial return to equity holders. In the context of this Standard, "operation" also includes an integrated set of activities that is capable of being conducted and managed for the purpose of providing a return in the form of dividends, lower costs or other economic benefits directly to investors or other owners, members or participants.

For the purposes of this Standard, owners is used broadly to include ~~any party with quantifiable ownership interests in an operation. This includes, but is not limited to,~~ holders of equity interests of investor-owned entities and owners or members of, or participants in, mutual entities.

A PBE ~~public-sector~~ combination under common control is a PBE ~~public-sector~~ combination in which all of the entities or operations involved are ultimately controlled by the same entity both before and after the PBE ~~public-sector~~ combination.

#### *Definitions related to amalgamations*

An amalgamation gives rise to a resulting entity and is either:

- (a) A PBE ~~public-sector~~ combination in which no party to the combination gains control of one or more operations; or
- (b) A PBE ~~public-sector~~ combination in which one party to the combination gains control of one or more operations, and in which there is evidence that the combination has the economic substance of an amalgamation.

(Paragraph AG1 provides additional guidance.)

The amalgamation date is the date on which the resulting entity obtains control of the combining operations.

A combining operation is an operation that combines with one or more other operations to form the resulting entity in an amalgamation.

A resulting entity is the entity that is the result of two or more operations combining in an amalgamation (paragraph AG1 provides additional guidance).

#### *Definitions relating to acquisitions*

An acquired operation is the operation that the acquirer gains control of in an acquisition.

An acquirer is the entity that gains control of one or more operations in an acquisition.

An acquisition is a PBE ~~public-sector~~ combination in which one party to the combination gains control of one or more operations, and there is evidence that the combination is not an amalgamation.

The acquisition date is the date on which the acquirer gains control of the acquired operation.

**Contingent consideration** is usually an obligation of the acquirer to transfer additional assets or equity interests to the former owners of an acquired operation as part of the exchange for control of the acquired operation if specified future events occur or conditions are met. However, contingent consideration also may give the acquirer the right to the return of previously transferred consideration if specified conditions are met.

**Goodwill** is an asset representing the future economic benefits arising from other assets acquired in an acquisition that are not individually identified and separately recognised.

Terms defined in other PBE Standards are used in this Standard with the same meaning as in those Standards, and are reproduced in the *Glossary of Defined Terms* published separately.

### Identifying a ~~PBE-public-sector~~ Combination

6. An entity shall determine whether a transaction or other event is a ~~PBE-public-sector~~ combination by applying the definitions in this Standard, which requires that the assets and liabilities constitute an operation. If the assets and liabilities do not constitute an operation, the entity shall account for the transaction or other event in accordance with other PBE Standards. Paragraphs AG2–AG9 provide guidance on identifying a ~~PBE-public-sector~~ combination.

### Classification of ~~PBEpublic-Sector~~ Combinations

7. If no party to a ~~PBE-public-sector~~ combination gains control of one or more operations as a result of the combination, the combination shall be classified as an amalgamation. Paragraphs AG10–AG18 provide guidance on determining whether one party to a ~~PBE-public-sector~~ combination gains control of one or more operations as a result of that combination.
8. If one party to a ~~PBE-public-sector~~ combination gains control of one or more operations as a result of the combination, an entity shall consider the economic substance of the combination in classifying the combination as either an amalgamation or an acquisition. A combination in which one party gains control of one or more operations shall be classified as an acquisition, unless it has the economic substance of an amalgamation.
9. In determining the classification of the ~~PBE public-sector~~ combination, an entity considers whether the resulting accounting treatment of the combination provides information that meets the objectives of financial reporting and that satisfies the qualitative characteristics (QCs). To assess the economic substance of the combination, an entity considers the indicators relating to consideration and to the decision-making process in paragraphs 12–13. These indicators, individually or in combination, will usually provide evidence that the economic substance of the combination is that of an amalgamation. A combination does not need to satisfy both of these indicators to be classified as an amalgamation. Paragraphs AG19–AG39 provide additional guidance.
10. An analysis of the indicators relating to consideration and to the decision-making process in paragraphs 12–13 will usually produce a conclusive result and provide sufficient evidence about the economic substance of the ~~PBEpublic-sector~~ combination to determine whether the combination is an amalgamation. In such circumstances, the resulting classification and the associated accounting treatment will ensure that users have access to information that meets the objectives of financial reporting and that satisfies the QCs.
11. In exceptional circumstances, after applying the indicators in paragraphs 12–13, the results may be inconclusive or may not provide sufficient evidence about the economic substance of the ~~PBE public-sector~~ combination. In such circumstances, an entity also considers which classification would provide information that best meets the objectives of financial reporting and that best satisfies the QCs, having regard to paragraph 14. Paragraphs AG40–AG41 provide additional guidance.

### Indicators that may Provide Evidence that the Combination is an Amalgamation

#### *Indicators Relating to Consideration*

12. The following indicators may provide evidence that the combination is an amalgamation:
  - (a) Consideration is paid for reasons other than to compensate those with an entitlement to the net assets of a transferred operation for giving up that entitlement (paragraphs AG27–AG28 provide additional guidance); or

- (b) Consideration is not paid to those with an entitlement to the net assets of a transferred operation. However, an entity is still required to consider the reasons why no consideration is paid (paragraphs AG29–AG30 provide additional guidance).~~;~~~~or~~
- (c) ~~Consideration is not paid because there is no one (whether an individual or an entity) with an entitlement to the net assets of a transferred entity (paragraph AG31 provides additional guidance).~~[Not used]

Agenda item 7.1 reference: Indicator in paragraph 12(c) (paras 10–17).

#### *Indicators Relating to the Decision-Making Process*

13. The following indicators may provide evidence that the combination is an amalgamation:

- (a) A ~~PBE public sector~~ combination is imposed by a third party without any party to the combination being involved in the decision-making process (paragraphs AG32–AG35 provide additional guidance);
- (b) A ~~PBE public sector~~ combination is subject to approval by each party's citizens through referenda (paragraph AG36 provides additional guidance); or
- (c) A ~~PBE public sector~~ combination under common control occurs (paragraphs AG37–AG39 provide additional guidance).

*Additional matters to be taken into account where the indicators relating to consideration and the decision-making process do not provide sufficient evidence to determine whether the combination is an amalgamation*

14. The analysis of the indicators relating to consideration and the decision-making process may, in exceptional circumstances, produce inconclusive results or not provide sufficient evidence to determine whether the combination is an amalgamation, based on the economic substance of the ~~PBE public sector~~ combination and the indicators in paragraphs 12–13. In such circumstances, an entity considers which classification and resulting accounting treatment would provide information that best meets the objectives of financial reporting. Paragraphs AG42–AG46 provide additional guidance. An entity also considers which classification and resulting accounting treatment would provide information that best satisfies the QCs of relevance, faithful representation, understandability, timeliness, comparability and verifiability. Paragraphs AG47–AG50 provide additional guidance.

### **Accounting for Amalgamations**

15. **A resulting entity shall account for each amalgamation by applying the modified pooling of interests method of accounting.**

### **The Modified Pooling of Interests Method of Accounting**

16. Applying the modified pooling of interests method of accounting requires:

- (a) Identifying the resulting entity;
- (b) Determining the amalgamation date;
- (c) Recognising and measuring the identifiable assets received, the liabilities assumed and any non-controlling interest in the combining operations, consistent with the requirements in PBE Standards; and
- (d) Recognising and measuring the components of net assets/equity and other adjustments from an amalgamation.

#### **Identifying the Resulting Entity**

17. **For each amalgamation, a resulting entity shall be identified.**

18. Paragraph 5 of this Standard defines a resulting entity as “the entity that is the result of two or more operations combining in an amalgamation.” The resulting entity shall thereafter be identified as the entity that obtains control of the combining operations as a result of the amalgamation.

### Determining the Amalgamation Date

19. **The resulting entity shall identify the amalgamation date, which is the date on which it obtains control of the combining operations.**
20. The date on which the resulting entity obtains control of the combining operations may be the date on which the resulting entity receives the assets and assumes the liabilities of the combining operations. It is possible that the resulting entity will not receive legal title to the assets or assume legal responsibility for the liabilities of the combining operations. In these circumstances, the resulting entity will often obtain control of the assets and liabilities of the combining operations on the date on which responsibility for the assets and liabilities is formally delegated to the resulting entity. However, the resulting entity might obtain control on a different date. For example, legislation or a written agreement may provide that the resulting entity obtains control of the assets and liabilities of the combining operations on a specified date. A resulting entity shall consider all pertinent facts and circumstances in identifying the amalgamation date.

### Recognising and Measuring the Identifiable Assets, Liabilities Assumed and any Non-Controlling Interests in the Combining Operations

#### *Recognition Principle*

21. **As of the amalgamation date, the resulting entity shall recognise the identifiable assets, liabilities and any non-controlling interests that are recognised in the financial statements of the combining operations as of the amalgamation date. Recognition of identifiable assets and liabilities received is subject to the conditions specified in paragraphs 22–23.**

#### *Recognition Conditions*

21.1 To qualify for recognition as part of applying the modified pooling of interests method, the identifiable assets and liabilities must meet the definitions of assets and liabilities in the *Public Benefit Entities' Conceptual Framework* at the amalgamation date. For example, costs that the resulting entity expects, but is not obliged, to incur in the future to effect its plan to exit an activity of a combining operation or to terminate the employment of or relocate a combining operation's employees are not liabilities at the amalgamation date. Therefore, the resulting entity does not recognise those costs as part of applying the modified pooling of interests method. Instead, the resulting entity recognises those costs in its post-combination financial statements in accordance with other PBE Standards.

22. **The effects of all transactions between the combining operations are eliminated in preparing the financial statements of the resulting entity (paragraphs AG51–AG52 provide related application guidance).**

23. ~~[Not used] To qualify for recognition as part of applying the modified pooling of interests method, the identifiable assets and liabilities must meet the definitions of assets and liabilities in the *Public Benefit Entities' Conceptual Framework* at the amalgamation date. For example, costs that the resulting entity expects, but is not obliged, to incur in the future to effect its plan to exit an activity of a combining operation or to terminate the employment of or relocate a combining operation's employees are not liabilities at the amalgamation date. Therefore, the resulting entity does not recognise those costs as part of applying the modified pooling of interests method. Instead, the resulting entity recognises those costs in its post-combination financial statements in accordance with other PBE Standards.~~

#### *Classifying or Designating Assets and Liabilities in an Amalgamation*

24. **At the amalgamation date, the resulting entity shall classify or designate the assets and liabilities received in an amalgamation using the classifications or designations previously applied by the combining operations. A resulting entity shall not adopt different classifications or designations on initial recognition, unless required to do so even if this is permitted by other PBE Standards.**
25. In some situations, PBE Standards provide for different accounting depending on how an entity classifies or designates a particular asset or liability. Examples of classifications or designations that the resulting entity shall make on the basis of the classifications or designations previously applied by the combining operations include but are not limited to:

- (a) Classification of particular financial assets and liabilities as measured at fair value or at amortised cost, in accordance with PBE IPSAS 29 *Financial Instruments: Recognition and Measurement*;<sup>3</sup>
- (b) Designation of a derivative instrument as a hedging instrument in accordance with PBE IPSAS 29; and
- (c) Assessment of whether an embedded derivative should be separated from a host contract in accordance with PBE IPSAS 29 (which is a matter of 'classification' as this Standard uses that term).

#### *Measurement Principle*

- 26. **The resulting entity shall measure the identifiable assets and liabilities of the combining operations at their carrying amounts in the financial statements of the combining operations as of the amalgamation date, subject to the requirements of paragraph 27 (paragraphs AG53–AG54 provide related application guidance).**
- 27. **As of the amalgamation date, the resulting entity shall adjust the carrying amounts of the identifiable assets and liabilities of the combining operations where required to conform to the resulting entity's accounting policies.**
- 28. The modified pooling of interests method results in a single combined resulting entity. A single uniform set of accounting policies, consistent with the requirements of PBE Standards, is adopted by that entity, and the carrying amounts of the identifiable assets and liabilities of the combining operations are adjusted, where required, to conform to those accounting policies.
- 29. The resulting entity shall measure any non-controlling interests in a combining operation at their carrying amounts in the financial statements of that combining operation as of the amalgamation date, adjusted for the non-controlling interests' proportionate share of the adjustments made in accordance with paragraph 27.
- 30. Paragraphs 33–35 specify the types of identifiable assets and liabilities that include items for which this Standard provides limited exceptions to the measurement principle.

#### *Exceptions to the Recognition or Measurement Principles*

- 31. This Standard provides limited exceptions to its recognition and measurement principles. Paragraphs 32–35 specify both the particular items for which exceptions are provided and the nature of those exceptions. The resulting entity shall account for those items by applying the requirements in paragraphs 32–35, which will result in some items being:
  - (a) Recognised either by applying recognition conditions in addition to those in paragraphs 22–23 or by applying the requirements of other PBE Standards, with results that differ from applying the recognition principle and conditions.
  - (b) Measured at an amount other than their amalgamation date carrying amounts.

#### *Exception to the Recognition Principle*

##### *Licences and Similar Rights Previously Granted by One Combining Operation to Another Combining Operation*

- 32. A licence or similar right, previously granted by one combining operation to another combining operation and recognised as an intangible asset by the recipient combining operation shall be recognised by the resulting entity as an intangible asset. The licence or similar right shall not be eliminated in accordance with paragraph 22 (paragraphs AG55–AG56 provide related application guidance).

#### *Exceptions to both the Recognition and Measurement Principles*

##### *Income Taxes (where Included in the Terms of the Amalgamation)*

- 33. Amalgamations involving public sector entities may result in a tax authority forgiving amounts of tax due as part of the terms of the amalgamation. The resulting entity shall not recognise any taxation items that

<sup>3</sup> If an entity applies this Standard and early adopts PBE IFRS 9 *Financial Instruments*, the references to PBE IPSAS 29 in this paragraph shall be read as a-references to PBE IFRS 9, including the classification of financial assets and financial liabilities in accordance with PBE IFRS 9.



are forgiven as a result of the terms of the amalgamation (paragraphs AG57–~~AG58~~ provide related application guidance).

34. ~~[Not used] The resulting entity shall recognise and measure any remaining taxation items included in or arising from an amalgamation in accordance with the relevant international or national accounting standard dealing with income taxes. The resulting entity shall recognise and measure any remaining revenue from taxation included in or arising from an amalgamation in accordance with PBE IPSAS 23 *Revenue from Non-Exchange Transactions (Taxes and Transfers)*.~~

Agenda item 7.1 reference: Tax forgiven (paras 22–27)
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#### Employee Benefits

35. The resulting entity shall recognise and measure a liability (or asset, if any) related to the combining operation's employee benefit arrangements in accordance with PBE IPSAS 39 *Employee Benefits*.

#### Recognising and Measuring Components of Net Assets/Equity Arising as a Result of an Amalgamation

36. An amalgamation does not give rise to goodwill (paragraphs AG59–AG60 provide related application guidance).
37. The resulting entity shall recognise within net assets/equity ~~the aggregate of amounts equal and opposite to the following items:~~
- (a) The carrying amounts of the combining operations' assets;
  - (b) The carrying amounts of the combining operations' liabilities; and
  - (c) The carrying amounts of the combining operations' non-controlling interests.
38. The resulting entity shall recognise within net assets/equity the corresponding adjustments in respect of:
- (a) The elimination of transactions between combining entities in accordance with paragraph 22;
  - (b) Adjustments made to the carrying amounts of the identifiable assets and liabilities of the combining operations where required to conform to the resulting entity's accounting policies, in accordance with paragraph 27; and
  - (c) Adjustments made in respect of the exceptions to the recognition and/or measurement principles, in accordance with paragraphs 32–35.
39. The resulting entity may present the amounts recognised within net assets/equity in accordance with paragraphs 37 and 38 as either:
- (a) A single opening balance; or
  - (b) As separate opening balances of the components of net assets/equity, including any components of the combining entities retained by the resulting entity.

#### Measurement Period

40. If the initial accounting for an amalgamation is incomplete by the end of the reporting period in which the amalgamation occurs, the resulting entity shall report in its financial statements provisional amounts for the items for which the accounting is incomplete. During the measurement period, the resulting entity shall retrospectively adjust the provisional amounts recognised at the amalgamation date to reflect new information obtained about facts and circumstances that existed as of the amalgamation date and, if known, would have affected the measurement of the amounts recognised as of that date. During the measurement period, the resulting entity shall also recognise additional assets or liabilities if new information is obtained about facts and circumstances that existed as of the amalgamation date and, if known, would have resulted in the recognition of those assets and liabilities as of that date. The measurement period ends as soon as the resulting entity receives the information it was seeking about facts and circumstances that existed as of the amalgamation date or learns that more information is not obtainable. However, the measurement period shall not exceed one year from the amalgamation date.



41. The measurement period is the period after the amalgamation date during which the resulting entity may adjust the provisional amounts recognised for an amalgamation. The measurement period provides the resulting entity with a reasonable time to obtain the information necessary to identify and measure the identifiable assets, liabilities and any non-controlling interest in the combining operations as of the amalgamation date in accordance with the requirements of this Standard. The information necessary to identify and measure the identifiable assets, liabilities and any non-controlling interest in the combining operations will generally be available at the amalgamation date. However, this may not be the case where combining operations have previously prepared their financial statements using different accounting policies.
42. The resulting entity recognises an increase (decrease) in the provisional amount recognised for an identifiable asset (liability) by adjusting components of net assets/equity recognised in accordance with paragraphs 37–38. However, new information obtained during the measurement period may sometimes result in an adjustment to the provisional amount of more than one asset or liability. For example, the resulting entity might have assumed a liability to pay damages related to an accident in one of the combining operation's facilities, part or all of which are covered by the combining operation's liability insurance policy. If the resulting entity obtains new information during the measurement period about the carrying amount of that liability, the adjustment to the gain or loss resulting from a change to the provisional amount recognised for the liability would be offset (in whole or in part) by a corresponding adjustment to the gain or loss resulting from a change to the provisional amount recognised for the claim receivable from the insurer.
43. During the measurement period, the resulting entity shall recognise adjustments to the provisional amounts as if the accounting for the amalgamation had been completed at the amalgamation date. Thus, the resulting entity shall revise comparative information for prior periods presented in financial statements as needed, including making any change in depreciation or amortisation recognised in completing the initial accounting.
44. After the measurement period ends, the resulting entity shall revise the accounting for an amalgamation only to correct an error in accordance with PBE IPSAS 3 *Accounting Policies, Changes in Accounting Estimates and Errors*.

#### **Amalgamation-Related Costs**

45. Amalgamation-related costs are costs the resulting entity or combining operations incur to effect an amalgamation. Those costs include advisory, legal, accounting, valuation and other professional or consulting fees; general administrative costs; and any costs of registering and issuing debt and equity securities. The resulting entity and combining operations shall account for amalgamation-related costs as expenses in the periods in which the costs are incurred and the services are received, with one exception. The costs to issue debt or equity securities shall be recognised in accordance with PBE IPSAS 28 *Financial Instruments: Presentation*, and PBE IPSAS 29<sup>4</sup>.

#### **Subsequent Measurement and Accounting**

46. In general, a resulting entity shall subsequently measure and account for assets and liabilities received and equity instruments issued in an amalgamation in accordance with other applicable PBE Standards for those items, depending on their nature. However, this Standard provides guidance on subsequently measuring and accounting for the following assets received and liabilities assumed or incurred in an amalgamation:
  - (a) Licences and similar rights previously granted by one combining operation to another combining operation;
  - (b) Transfers, concessionary loans and similar benefits received by a combining operation on the basis of criteria that change as a result of an amalgamation; and
  - (c) Income taxes (where not included in the terms of the amalgamation).

#### *Licences and Similar Rights Previously Granted by One Combining Operation to Another Combining Operation*

47. A licence or similar right, previously granted by one combining operation to another combining operation and recognised as an intangible asset shall be amortised over the remaining period of the binding

<sup>4</sup> If an entity applies this Standard and early adopts PBE IFRS 9 *Financial Instruments*, the references to PBE IPSAS 29 in this paragraph shall be read as a reference to PBE IFRS 9.

arrangement in which the right was granted, where the right was granted for a finite period. Where the right was granted for an indefinite period, the resulting entity shall test the right for impairment at least annually, and whenever there is an indication that the right may be impaired. A resulting entity that subsequently sells this licence or similar right to a third party shall include the carrying amount of the intangible asset in determining the gain or loss on the sale.

*Transfers, Concessionary Loans and Similar Benefits Received by a Combining Operation on the Basis of Criteria that may Change as a Result of an Amalgamation*

48. A transfer, concessionary loan or similar benefit, previously received by a combining operation on the basis of criteria that change as a result of an amalgamation, shall be reassessed prospectively in accordance with other PBE Standards (paragraphs AG61–AG63 provide related application guidance).

*Income Taxes (Where not Included in the terms of the Amalgamation)*

49. Amalgamations involving public sector entities may result in a tax authority forgiving amounts of tax subsequent to the amalgamation. The resulting entity shall account for the tax forgiven prospectively in accordance with PBE IAS 12 ~~the relevant international or national accounting standard dealing with income taxes.~~

**Presentation of Financial Statements**

50. ~~If following a PBE combination~~ **Except where a the** resulting entity is ~~not~~ a new **legal** entity ~~following a public sector combination~~, the resulting entity's first set of financial statements following the amalgamation shall comprise:
- (a) An opening statement of financial position as of the amalgamation date;
  - (b) A statement of financial position as at the reporting date;
  - (c) ~~A statement of financial performance~~ **statement of comprehensive revenue and expense** for the period from the amalgamation date to the reporting date;
  - (d) A statement of changes in net assets/equity for the period from the amalgamation date to the reporting date;
  - (e) A cash flow statement for the period from the amalgamation date to the reporting date;
  - (f) ~~If the entity makes publicly available its approved budget, a comparison of budget and actual amounts for the period from the amalgamation date to the reporting date, either as a separate additional financial statement or as a budget column in the financial statements~~ **When a public sector entity has published general purpose prospective financial statements for the period from the amalgamation date to the reporting date, the information specified in paragraph 148.1 of PBE IPSAS 1 shall be presented on the face of the financial statements or as a separate statement. When a not-for-profit entity has published general purpose prospective financial statements for the period from the amalgamation date to the reporting date, the information specified in paragraph 148.1 of PBE IPSAS 1 shall be presented on the face of the financial statements, as a separate statement or in the notes; and**
  - (g) Notes, comprising a summary of significant accounting policies and other explanatory notes.
51. ~~If following a PBE combination~~ **Where a the** resulting entity is not a new **legal** entity ~~following a public sector combination~~, the resulting entity shall disclose:
- (a) The amounts recognised of each major class of assets and liabilities, and components of net assets/equity from combining operations included in the resulting entity;
  - (b) Any adjustments made to components of net assets/equity where required to conform the accounting policies of the combining operations with those of the resulting entity; and
  - (c) Any adjustments made to eliminate transactions between the combining operations.
52. Subject to the requirements in paragraphs 54 and 56, the resulting entity is permitted but not required to present financial statements for periods prior to the amalgamation date (paragraphs AG64–AG65 provide related application guidance). Where a resulting entity elects to present financial statements for periods prior to the amalgamation date, it shall disclose the information required by paragraph 54(g).

The RDR concessions for amalgamations will be considered later. For this meeting, we are seeking the Board's feedback on the RDR concessions for acquisitions.

## Disclosures

53. **The resulting entity shall disclose information that enables users of its financial statements to evaluate the nature and financial effect of an amalgamation.**

54. To meet the objective in paragraph 53, the resulting entity shall disclose the following information for each amalgamation that occurs during the reporting period:

- (a) The name and a description of each combining operation.
- (b) The amalgamation date.
- (c) The primary reasons for the amalgamation including, where applicable, the legal basis for the amalgamation.
- (d) The amounts recognised as of the amalgamation date for each major class of assets and liabilities transferred.
- (e) The adjustments made to the carrying amounts of assets and liabilities recorded by each combining operation as of the amalgamation date:
  - (i) To eliminate the effect of transactions between combining operations in accordance with paragraph 22; and
  - (ii) To conform to the resulting entity's accounting policies in accordance with paragraph 27.
- (f) An analysis of net assets/equity, including any components that are presented separately, and any significant adjustments such as revaluation surpluses or deficits, recognised in accordance with paragraphs 37–38.
- (g) If a resulting entity elects to present financial statements for periods prior to the amalgamation date in accordance with paragraph 52, the resulting entity shall disclose the following information for each combining operation:
  - (i) A statement of financial position as at the end of the prior period(s);
  - (ii) A ~~statement of financial performance~~ statement of comprehensive revenue and expense for the prior period(s);
  - (iii) A statement of changes in net assets/equity for the prior period(s);
  - (iv) A cash flow statement for the prior period(s); and
  - (v) Notes, comprising a summary of significant accounting policies and other explanatory notes.

The resulting entity shall not restate this information, but shall disclose the information on the same basis as previously used in the combining operations' financial statements. The resulting entity shall disclose the significant differences in accounting policies applied by the resulting entity and the previously reported combining operations' financial statements basis on which this information is presented.

- (h) If, at the time the financial statements of the resulting entity are authorised for issue, the last reporting date of any of the combining operations does not immediately precede the amalgamation date, the resulting entity shall disclose the following information:
  - (i) The amounts of revenue and expense, and the surplus or deficit of each combining operation from the last reporting date of the combining operations until the amalgamation date. The amounts of revenue shall be analysed in a manner appropriate to the entity's operations, in accordance with paragraph 108 of PBE IPSAS 1 *Presentation of Financial Statements*. The amounts of expense shall be analysed using a classification based on either the nature of expenses or their function within the entity, whichever provides information that is faithfully representative and more relevant, in accordance with paragraph 109 of PBE IPSAS 1.
  - (ii) The amounts reported by each combining operation immediately prior to the amalgamation date for each major class of assets and liabilities.

- (iii) The amounts reported by each combining operation immediately prior to the amalgamation date in net assets/equity.

The resulting entity is not required to disclose this information where it has elected to present financial statements for periods prior to the amalgamation date as specified in subparagraph (g) above.

55. **The resulting entity shall disclose information that enables users of its financial statements to evaluate the financial effects of adjustments recognised in the current reporting period that relate to amalgamations that occurred in the period or previous reporting periods.**
56. To meet the objective in paragraph 55, the resulting entity shall disclose the following information:
  - (a) If the initial accounting for an amalgamation is incomplete (see paragraph 40) for particular assets or liabilities, and the amounts recognised in the financial statements for the amalgamation thus have been determined only provisionally:
    - (i) The reasons why the initial accounting for the amalgamation is incomplete;
    - (ii) The assets or liabilities for which the initial accounting is incomplete; and
    - (iii) The nature and amount of any measurement period adjustments recognised during the reporting period in accordance with paragraph 43.
  - (b) If amounts of tax due are forgiven as a result of the terms of the amalgamation (see paragraphs 33–34):
    - (i) The amount of tax due that was forgiven; and
    - (ii) Where the resulting entity is the tax authority, details of the adjustment made to tax receivable.
57. If the specific disclosures required by this and other PBE Standards do not meet the objectives set out in paragraphs 53 and 55, the resulting entity shall disclose whatever additional information is necessary to meet those objectives.

## Accounting for Acquisitions

58. **An acquirer shall account for each acquisition by applying the acquisition method of accounting.**

### The Acquisition Method of Accounting

59. Applying the acquisition method of accounting requires:
  - (a) Identifying the acquirer;
  - (b) Determining the acquisition date;
  - (c) Recognising and measuring the identifiable assets acquired, the liabilities assumed and any non-controlling interest in the acquired operation; and
  - (d) Recognising and measuring goodwill, a gain or a loss from an acquisition.

#### Identifying the Acquirer

60. **For each acquisition, the party to the combination that gains control of one or more operations shall be identified as the acquirer.**
61. The party to the combination that gains control of one or more operations is identified when determining the classification of the ~~PBEpublic-sector~~ combination in accordance with paragraphs 7, 8 and AG10–AG18.

#### Determining the Acquisition Date

62. **The acquirer shall identify the acquisition date, which is the date on which it obtains control of the acquired operation.**
63. The date on which the acquirer obtains control of the acquired operation is generally the date on which the acquirer legally transfers the consideration and/or acquires the assets and assumes the liabilities of the acquired operation—the closing date. However, the acquirer might obtain control on a date that is either

earlier or later than the closing date. For example, the acquisition date precedes the closing date if a written agreement provides that the acquirer obtains control of the acquired operation on a date before the closing date. An acquirer shall consider all pertinent facts and circumstances in identifying the acquisition date.

### **Recognising and Measuring the Identifiable Assets Acquired, the Liabilities Assumed and any Non-Controlling Interest in the Acquired Operation**

#### *Recognition Principle*

64. **As of the acquisition date, the acquirer shall recognise, separately from any goodwill recognised, the identifiable assets acquired, the liabilities assumed and any non-controlling interest in the acquired operation. Recognition of identifiable assets acquired and liabilities assumed is subject to the conditions specified in paragraphs 65 and 66.**

#### *Recognition Conditions*

65. To qualify for recognition as part of applying the acquisition method, the identifiable assets acquired and liabilities assumed must meet the definitions of assets and liabilities in the *Public Benefit Entities' Conceptual Framework* at the acquisition date, and be capable of being measured in a way that achieves the qualitative characteristics and takes account of constraints on information in general purpose financial reporting. For example, costs the acquirer expects but is not obliged to incur in the future to effect its plan to exit an activity of an acquired operation or to terminate the employment of or relocate an acquired operation's employees are not liabilities at the acquisition date. Therefore, the acquirer does not recognise those costs as part of applying the acquisition method. Instead, the acquirer recognises those costs in its post-combination financial statements in accordance with other PBE Standards.
66. In addition, to qualify for recognition as part of applying the acquisition method, the identifiable assets acquired and liabilities assumed must be part of what the acquirer and the acquired operation (or its former owners) exchanged in the acquisition transaction rather than the result of separate transactions. The acquirer shall apply the guidance in paragraphs 109–111 to determine which assets acquired or liabilities assumed are part of the exchange for the acquired operation and which, if any, are the result of separate transactions to be accounted for in accordance with their nature and the applicable PBE Standards.
67. The acquirer's application of the recognition principle and conditions may result in recognising some assets and liabilities that the acquired operation had not previously recognised as assets and liabilities in its financial statements. For example, the acquirer recognises the acquired identifiable intangible assets, such as a patent or a customer relationship, that the acquired operation did not recognise as assets in its financial statements because it developed them internally and charged the related costs to expense.
68. Paragraphs AG72–AG84 provide guidance on recognising operating leases and intangible assets. Paragraphs 76–82 specify the types of identifiable assets and liabilities that include items for which this Standard provides limited exceptions to the recognition principle and conditions.

#### *Classifying or Designating Identifiable Assets Acquired and Liabilities Assumed in an Acquisition*

69. **At the acquisition date, the acquirer shall classify or designate the identifiable assets acquired and liabilities assumed as necessary to subsequently apply other PBE Standards. The acquirer shall make those classifications or designations on the basis of the terms of the binding arrangement (including contractual terms), economic conditions, its operating or accounting policies and other pertinent conditions as they exist at the acquisition date.**
70. In some situations, PBE Standards provide for different accounting depending on how an entity classifies or designates a particular asset or liability. Examples of classifications or designations that the acquirer shall make on the basis of the pertinent conditions as they exist at the acquisition date include but are not limited to:
- (a) Classification of particular financial assets and liabilities as measured at fair value or at amortised cost, in accordance with PBE IPSAS 29;<sup>5</sup>
  - (b) Designation of a derivative instrument as a hedging instrument in accordance with PBE IPSAS 29; and

<sup>5</sup> If an entity applies this Standard and early adopts PBE IFRS 9 *Financial Instruments*, the references to PBE IPSAS 29 in this paragraph shall be read as a reference to PBE IFRS 9.

- (c) Assessment of whether an embedded derivative should be separated from a host contract in accordance with PBE IPSAS 29 (which is a matter of ‘classification’ as this Standard uses that term).
71. This Standard provides two exceptions to the principle in paragraph 69:
- (a) Classification of a lease arrangement as either an operating lease or a finance lease in accordance with PBE IPSAS 13 *Leases*; and
  - (b) Classification of a contract as an insurance contract in accordance with PBE IFRS 4 Insurance Contracts~~the relevant international or national accounting standard dealing with insurance contracts.~~

The acquirer shall classify those binding arrangements on the basis of the terms and other factors at the inception of the binding arrangement (or, if the terms of the binding arrangement have been modified in a manner that would change its classification, at the date of that modification, which might be the acquisition date).

#### *Measurement Principle*

72. **The acquirer shall measure the identifiable assets acquired and the liabilities assumed at their acquisition-date fair values.**
73. For each acquisition, the acquirer shall measure at the acquisition date components of non-controlling interests in the acquired operation that are present ownership interests and entitle their holders to a proportionate share of the entity’s net assets in the event of liquidation at either:
- (a) Fair value; or
  - (b) The present ownership instruments’ proportionate share in the recognised amounts of the acquired operation’s identifiable net assets.

All other components of non-controlling interests shall be measured at their acquisition-date fair values, unless another measurement basis is required by PBE Standards.

74. Paragraphs 78–84 specify the types of identifiable assets and liabilities that include items for which this Standard provides limited exceptions to the measurement principle.

#### *Exceptions to the Recognition or Measurement Principles*

75. This Standard provides limited exceptions to its recognition and measurement principles. Paragraphs 76–84 specify both the particular items for which exceptions are provided and the nature of those exceptions. The acquirer shall account for those items by applying the requirements in paragraphs 76–84, which will result in some items being:
- (a) Recognised either by applying recognition conditions in addition to those in paragraphs 65–66 or by applying the requirements of other PBE Standards, with results that differ from applying the recognition principle and conditions.
  - (b) Measured at an amount other than their acquisition-date fair values.

#### *Exception to the Recognition Principle*

##### *Contingent Liabilities*

76. PBE IPSAS 19 *Provisions, Contingent Liabilities and Contingent Assets*, defines a contingent liability as:
- (a) A possible obligation that arises from past events, and whose existence will be confirmed only by the occurrence or non-occurrence of one or more uncertain future events not wholly within the control of the entity; or
  - (b) A present obligation that arises from past events, but is not recognised because:
    - (i) It is not probable that an outflow of resources embodying economic benefits or service potential will be required to settle the obligation; or
    - (ii) The amount of the obligation cannot be measured with sufficient reliability.



77. The requirements in PBE IPSAS 19 do not apply in determining which contingent liabilities to recognise as of the acquisition date. Instead, the acquirer shall recognise as of the acquisition date a contingent liability assumed in an acquisition where consideration is transferred if it is a present obligation that arises from past events and its fair value can be measured reliably<sup>6</sup>. Therefore, contrary to PBE IPSAS 19, the acquirer recognises a contingent liability assumed in an acquisition where consideration is transferred at the acquisition date even if it is not probable that an outflow of resources embodying economic benefits or service potential will be required to settle the obligation. Paragraph 115 provides guidance on the subsequent accounting for contingent liabilities.

#### Exceptions to both the Recognition and Measurement Principles

##### Income Taxes (where Included in the Terms of the Acquisition)

78. Acquisitions by a ~~PBE public sector entity~~ may result in a tax authority forgiving amounts of tax due as part of the terms of the acquisition. The acquirer shall not recognise any taxation items that are forgiven as a result of the terms of the acquisition (paragraphs AG85 and –AG87 provide related application guidance).
79. ~~[Not used] The acquirer shall recognise and measure any remaining taxation items included in or arising from an acquisition in accordance with the relevant international or national accounting standard dealing with income taxes. The acquirer entity shall recognise and measure any remaining revenue from taxation included in or arising from an acquisition in accordance with IPSAS 23.~~
- 79.1 The acquirer shall recognise and measure a deferred tax asset or liability arising from the assets acquired and liabilities assumed in a PBE combination in accordance with PBE IAS 12.
- 79.2 The acquirer shall account for the potential tax effects of temporary differences and carryforwards of the acquired operation that exist at the acquisition date or arise as a result of the acquisition in accordance with PBE IAS 12.

Agenda item 7.1 reference: Tax forgiven (paras 22–27)
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##### Employee Benefits

80. The acquirer shall recognise and measure a liability (or asset, if any) related to the acquired operation's employee benefit arrangements in accordance with PBE IPSAS 39.

##### Indemnification Assets

81. The seller in an acquisition may contractually indemnify the acquirer for the outcome of a contingency or uncertainty related to all or part of a specific asset or liability. For example, the seller may indemnify the acquirer against losses above a specified amount on a liability arising from a particular contingency; in other words, the seller will guarantee that the acquirer's liability will not exceed a specified amount. As a result, the acquirer obtains an indemnification asset. The acquirer shall recognise an indemnification asset at the same time that it recognises the indemnified item measured on the same basis as the indemnified item, subject to the need for a valuation allowance for uncollectible amounts. Therefore, if the indemnification relates to an asset or a liability that is recognised at the acquisition date and measured at its acquisition-date fair value, the acquirer shall recognise the indemnification asset at the acquisition date measured at its acquisition-date fair value. For an indemnification asset measured at fair value, the effects of uncertainty about future cash flows because of collectibility considerations are included in the fair value measure and a separate valuation allowance is not necessary (paragraph AG88 provides related application guidance).
82. In some circumstances, the indemnification may relate to an asset or a liability that is an exception to the recognition or measurement principles. For example, an indemnification may relate to a contingent liability that is not recognised at the acquisition date because its fair value is not reliably measurable at that date. Alternatively, an indemnification may relate to an asset or a liability, for example, one that results from an employee benefit, that is measured on a basis other than acquisition-date fair value. In those circumstances, the indemnification asset shall be recognised and measured using assumptions consistent with those used to measure the indemnified item, subject to management's assessment of the collectibility of the

<sup>6</sup> Information that is reliable is free from material error and bias, and can be depended on by users to faithfully represent that which it purports to represent or could reasonably be expected to represent. Paragraph BC10+6 of PBE IPSAS 1 discusses the transitional approach to the explanation of reliability.

indemnification asset and any contractual limitations on the indemnified amount. Paragraph 116 provides guidance on the subsequent accounting for an indemnification asset.

#### Exceptions to the Measurement Principle

##### Reacquired Rights

83. The acquirer shall measure the value of a reacquired right recognised as an intangible asset on the basis of the remaining term of the related binding arrangement regardless of whether market participants would consider potential renewals of binding arrangements when measuring its fair value. Paragraphs AG79–AG80 provide related application guidance.

##### Share-Based Payment Transactions

84. The acquirer shall measure a liability or an equity instrument related to share-based payment transactions of the acquired operation or the replacement of an acquired operation's share-based payment transactions with share-based payment transactions of the acquirer in accordance with the relevant international or national accounting standard dealing with share-based payments.

##### Assets Held for Sale

- 84.1 The acquirer shall measure an acquired non-current asset (or disposal group) that is classified as held for sale at the acquisition date in accordance with PBE IFRS 5 *Non-current Assets Held for Sale and Discontinued Operations* at fair value less costs to sell in accordance with paragraphs 15–18 of that Standard.

#### Recognising and Measuring Goodwill or a Gain from a Bargain Purchase

85. The acquirer shall recognise goodwill as of the acquisition date measured as the excess of (a) over (b) below, subject to the requirements of paragraph 86:

- (a) The aggregate of:
  - (i) The consideration transferred measured in accordance with this Standard, which generally requires acquisition-date fair value (see paragraph 95);
  - (ii) The amount of any non-controlling interest in the acquired operation measured in accordance with this Standard; and
  - (iii) In an acquisition achieved in stages (see paragraphs 99–100), the acquisition-date fair value of the acquirer's previously held equity interest in the acquired operation.
- (b) The net of the acquisition-date amounts of the identifiable assets acquired and the liabilities assumed measured in accordance with this Standard.

86. The acquirer shall recognise goodwill only to the extent that the acquisition will result in:

- (a) The generation of cash inflows (such as the acquisition of a cash-generating operation); and/or
- (b) A reduction in the net cash outflows of the acquirer.

**An acquirer shall recognise any further excess of (a) over (b) in paragraph 85 above as a loss in surplus or deficit. Paragraph AG93 provides related application guidance.**

87. In an acquisition in which the acquirer and the acquired operation (or its former owners) exchange only equity interests, the acquisition-date fair value of the acquired operation's equity interests may be more reliably measurable than the acquisition-date fair value of the acquirer's equity interests. If so, the acquirer shall determine the amount of goodwill by using the acquisition-date fair value of the acquired operation's equity interests instead of the acquisition-date fair value of the equity interests transferred. To determine the amount of goodwill in an acquisition in which no consideration is transferred in those situations covered in paragraphs 101 and 102, the acquirer shall use the acquisition-date fair value of the acquirer's interest in the acquired operation in place of the acquisition-date fair value of the consideration transferred (paragraph 85(a)(i)). Paragraph AG94–AG97 provides related application guidance.

##### *Bargain Purchases*

88. Occasionally in a PBE–public-sector combination classified as an acquisition, an acquirer will make a bargain purchase, which is an acquisition in which the amount in paragraph 85(b) exceeds the aggregate



of the amounts specified in paragraph 85(a). If that excess remains after applying the requirements in paragraph 90, the acquirer shall recognise the resulting gain in surplus or deficit on the acquisition date. The gain shall be attributed to the acquirer.

89. A bargain purchase might happen, for example, in an acquisition that is a forced sale in which the seller is acting under economic compulsion. However, the recognition or measurement exceptions for particular items discussed in paragraphs 76–84 may also result in recognising a gain (or change the amount of a recognised gain) on a bargain purchase.
90. Before recognising a gain on a bargain purchase, the acquirer shall reassess whether it has correctly identified all of the assets acquired and all of the liabilities assumed and shall recognise any additional assets or liabilities that are identified in that review. The acquirer shall then review the procedures used to measure the amounts this Standard requires to be recognised at the acquisition date for all of the following:
  - (a) The identifiable assets acquired and liabilities assumed;
  - (b) The non-controlling interest in the acquired operation, if any;
  - (c) For an acquisition achieved in stages, the acquirer's previously held equity interest in the acquired operation; and
  - (d) The consideration transferred.

The objective of the review is to ensure that the measurements appropriately reflect consideration of all available information as of the acquisition date.

91. In the PBE public sector, an entity sometimes obtains control of an operation in a non-exchange transaction in which it transfers consideration that is not approximately equal to the fair value of the acquired operation. Such circumstances include, but are not limited to:
  - (a) Compensated seizures of operations or entities; and
  - (b) The transfer of an operation to the acquirer by a donor for nominal consideration.
92. Where the economic substance of the PBE public sector combination is that of an acquisition, such non-exchange acquisitions are treated as bargain purchases and accounted for in accordance with paragraphs 88–90.

#### *A Non-Exchange Acquisition without the Transfer of Consideration*

93. In the public benefit entity sector, an entity sometimes obtains control of an operation in a non-exchange transaction in which it transfers no consideration. Such circumstances include, but are not limited to:
  - (a) Uncompensated seizures of operations or entities (also known as forced nationalisations).
  - (b) The transfer of an operation to the entity by a donor for no consideration. Such transfers may take the form of a bequest.

And

  - (c) The transfer of an operation to the entity where the operation has net liabilities. The entity may accept the transfer of net liabilities to prevent the cessation of the operation. Such transactions are sometimes known as “bailouts”.
94. Where the economic substance of the PBE public sector combination is that of an acquisition, the acquirer that obtains control of an acquired operation in a non-exchange transaction in which it transfers no consideration does not recognise goodwill. The acquirer recognises a gain or a loss in surplus or deficit, ~~in accordance with paragraph 86.~~

#### *Consideration Transferred*

95. The consideration transferred in an acquisition shall be measured at fair value, which shall be calculated as the sum of the acquisition-date fair values of the assets transferred by the acquirer, the liabilities incurred by the acquirer to former owners of the acquired operation and the equity interests issued by the acquirer. (However, any portion of the acquirer's share-based payment awards exchanged for awards held by the acquired operation's employees that is included in consideration transferred in the acquisition shall be measured in accordance with paragraph 84 rather than at fair value.) Examples of potential forms of consideration include cash, other assets, an operation or a controlled entity of the acquirer, contingent

consideration, ordinary or preference equity instruments, options, warrants and member interests of mutual entities.

96. The consideration transferred may include assets or liabilities of the acquirer that have carrying amounts that differ from their fair values at the acquisition date (for example, non-monetary assets or an operation of the acquirer). If so, the acquirer shall remeasure the transferred assets or liabilities to their fair values as of the acquisition date and recognise the resulting gains or losses, if any, in surplus or deficit. However, sometimes the transferred assets or liabilities remain within the combined entity after the acquisition (for example, because the assets or liabilities were transferred to the acquired operation rather than to its former owners), and the acquirer therefore retains control of them. In that situation, the acquirer shall measure those assets and liabilities at their carrying amounts immediately before the acquisition date and shall not recognise a gain or loss in surplus or deficit on assets or liabilities it controls both before and after the acquisition.

#### Contingent Consideration

97. The consideration the acquirer transfers in exchange for the acquired operation includes any asset or liability resulting from a contingent consideration arrangement (see paragraph 95). The acquirer shall recognise the acquisition-date fair value of contingent consideration as part of the consideration transferred in exchange for the acquired operation.
98. The acquirer shall classify an obligation to pay contingent consideration that meets the definition of a financial instrument as a financial liability or as a component of net assets/equity on the basis of the definitions of an equity instrument and a financial liability in paragraph 9 of PBE IPSAS 28. The acquirer shall classify as an asset a right to the return of previously transferred consideration if specified conditions are met. Paragraph 117 provides guidance on the subsequent accounting for contingent consideration.

#### An Acquisition Achieved in Stages

99. An acquirer sometimes obtains control of an acquired operation in which it held an equity interest immediately before the acquisition date. For example, on 31 December 20X1, Entity A holds a 35 percent non-controlling equity interest in Entity B. On that date, Entity A purchases an additional 40 percent interest in Entity B, which gives it control of Entity B. This Standard refers to such a transaction as an acquisition achieved in stages, sometimes also referred to as a step acquisition.
100. In an acquisition achieved in stages, the acquirer shall remeasure its previously held equity interest in the acquired operation at its acquisition-date fair value and recognise the resulting gain or loss, if any, in surplus or deficit or in ~~net assets/equity~~other comprehensive revenue and expense, as appropriate. In prior reporting periods, the acquirer may have recognised changes in the value of its equity interest in the acquired operation in ~~net assets/equity~~other comprehensive revenue and expense (for example, because the investment was classified as available for sale). If so, the amount that was recognised in ~~net assets/equity~~other comprehensive revenue and expense shall be recognised on the same basis as would be required if the acquirer had disposed directly of the previously held equity interest.

#### Additional Guidance for Applying the Acquisition Method where an Acquisition is Achieved Through Changes in Voting Rights, by Contract Alone, and Similar Circumstances in which no Consideration is Transferred

##### *An Acquisition Achieved Through Changes in Voting Rights, by Contract Alone, and Similar Circumstances not Involving the Transfer of Consideration*

101. An acquirer sometimes obtains control of an acquired operation without transferring consideration. The acquisition method of accounting for an acquisition applies to those ~~PBE~~public sector combinations. Such circumstances include:
- (a) The acquired operation repurchases a sufficient number of its own shares for an existing investor (the acquirer) to obtain control.
  - (b) Minority veto rights lapse that previously kept the acquirer from controlling an acquired operation in which the acquirer held the majority voting rights.
  - (c) The acquirer and acquired operation agree to combine their operations by contract alone. The acquirer transfers no consideration in exchange for control of an acquired operation and holds no

~~equity quantifiable ownership~~ interests in the acquired operation, either on the acquisition date or previously.

102. In an acquisition achieved by contract alone, the acquirer shall attribute to the owners of the acquired operation the amount of the acquired operation's net assets recognised in accordance with this Standard. In other words, the ~~equity quantifiable ownership~~ interests in the acquired operation held by parties other than the acquirer are a non-controlling interest in the acquirer's post-combination financial statements even if the result is that all of the ~~equity quantifiable ownership~~ interests in the acquired operation are attributed to the non-controlling interest.

### Measurement Period

103. **If the initial accounting for an acquisition is incomplete by the end of the reporting period in which the acquisition occurs, the acquirer shall report in its financial statements provisional amounts for the items for which the accounting is incomplete. During the measurement period, the acquirer shall retrospectively adjust the provisional amounts recognised at the acquisition date to reflect new information obtained about facts and circumstances that existed as of the acquisition date and, if known, would have affected the measurement of the amounts recognised as of that date. During the measurement period, the acquirer shall also recognise additional assets or liabilities if new information is obtained about facts and circumstances that existed as of the acquisition date and, if known, would have resulted in the recognition of those assets and liabilities as of that date. The measurement period ends as soon as the acquirer receives the information it was seeking about facts and circumstances that existed as of the acquisition date or learns that more information is not obtainable. However, the measurement period shall not exceed one year from the acquisition date.**
104. The measurement period is the period after the acquisition date during which the acquirer may adjust the provisional amounts recognised for an acquisition. The measurement period provides the acquirer with a reasonable time to obtain the information necessary to identify and measure the following as of the acquisition date in accordance with the requirements of this Standard:
- (a) The identifiable assets acquired, liabilities assumed and any non-controlling interest in the acquired operation;
  - (b) The consideration transferred for the acquired operation (or the other amount used in measuring goodwill);
  - (c) In an acquisition achieved in stages, the equity interest in the acquired operation previously held by the acquirer; and
  - (d) The resulting goodwill, loss, or gain on a bargain purchase.
105. The acquirer shall consider all pertinent factors in determining whether information obtained after the acquisition date should result in an adjustment to the provisional amounts recognised or whether that information results from events that occurred after the acquisition date. Pertinent factors include the date when additional information is obtained and whether the acquirer can identify a reason for a change to provisional amounts. Information that is obtained shortly after the acquisition date is more likely to reflect circumstances that existed at the acquisition date than is information obtained several months later. For example, unless an intervening event that changed its fair value can be identified, the sale of an asset to a third party shortly after the acquisition date for an amount that differs significantly from its provisional fair value measured at that date is likely to indicate an error in the provisional amount.
106. The acquirer recognises an increase (decrease) in the provisional amount recognised for an identifiable asset (liability) by means of a decrease (increase) in goodwill subject to the requirements for recognition of goodwill in paragraph 86. However, new information obtained during the measurement period may sometimes result in an adjustment to the provisional amount of more than one asset or liability. For example, the acquirer might have assumed a liability to pay damages related to an accident in one of the acquired operation's facilities, part or all of which are covered by the acquired operation's liability insurance policy. If the acquirer obtains new information during the measurement period about the acquisition-date fair value of that liability, the adjustment to goodwill resulting from a change to the provisional amount recognised for the liability would be offset (in whole or in part) by a corresponding adjustment to goodwill resulting from a change to the provisional amount recognised for the claim receivable from the insurer.

107. During the measurement period, the acquirer shall recognise adjustments to the provisional amounts as if the accounting for the acquisition had been completed at the acquisition date. Thus, the acquirer shall revise comparative information for prior periods presented in financial statements as needed, including making any change in depreciation, amortisation or other income effects recognised in completing the initial accounting.
108. After the measurement period ends, the acquirer shall revise the accounting for an acquisition only to correct an error in accordance with PBE IPSAS 3.

#### **Determining what is Part of the Acquisition Transaction**

109. **The acquirer and the acquired operation may have a pre-existing relationship or other arrangement before negotiations for the acquisition began, or they may enter into an arrangement during the negotiations that is separate from the acquisition. In either situation, the acquirer shall identify any amounts that are not part of what the acquirer and the acquired operation (or its former owners) exchanged in the acquisition, i.e., amounts that are not part of the exchange for the acquired operation. The acquirer shall recognise as part of applying the acquisition method only the consideration transferred for the acquired operation and the assets acquired and liabilities assumed in the exchange for the acquired operation. Separate transactions shall be accounted for in accordance with the relevant PBE Standards.**
110. A transaction entered into by or on behalf of the acquirer or primarily for the benefit of the acquirer or the combined entity, rather than primarily for the benefit of the acquired operation (or its former owners) before the acquisition, is likely to be a separate transaction. The following are examples of separate transactions that are not to be included in applying the acquisition method:
- (a) A transaction that in effect settles pre-existing relationships between the acquirer and acquired operation;
  - (b) A transaction that remunerates employees or former owners of the acquired operation for future services; and
  - (c) A transaction that reimburses the acquired operation or its former owners for paying the acquirer's acquisition-related costs.

Paragraphs AG99–AG106 provide related application guidance.

#### *Acquisition-Related Costs*

111. Acquisition-related costs are costs the acquirer incurs to effect an acquisition. Those costs include finder's fees; advisory, legal, accounting, valuation and other professional or consulting fees; general administrative costs, including the costs of maintaining an internal acquisitions department; and costs of registering and issuing debt and equity securities. The acquirer shall account for acquisition-related costs as expenses in the periods in which the costs are incurred and the services are received, with one exception. The costs to issue debt or equity securities shall be recognised in accordance with PBE IPSAS 28 and PBE IPSAS 29<sup>7</sup>.

#### **Subsequent Measurement and Accounting**

112. **In general, an acquirer shall subsequently measure and account for assets acquired, liabilities assumed or incurred and equity instruments issued in an acquisition in accordance with other applicable PBE Standards for those items, depending on their nature. However, this Standard provides guidance on subsequently measuring and accounting for the following assets acquired, liabilities assumed or incurred and equity instruments issued in an acquisition:**
- (a) **Reacquired rights;**
  - (b) **Contingent liabilities recognised as of the acquisition date;**
  - (c) **Indemnification assets;**
  - (d) **Contingent consideration; and**
  - (e) **Income taxes (where not included in the terms of the acquisition).**

<sup>7</sup> If an entity applies this Standard and early adopts PBE IFRS 9 *Financial Instruments*, the references to PBE IPSAS 29 in this paragraph shall be read as a reference to PBE IFRS 9.

**Paragraphs AG107–AG108 provide related application guidance.***Reacquired Rights*

113. A reacquired right recognised as an intangible asset shall be amortized over the remaining period of the binding arrangement in which the right was granted, where the right was granted for a finite period. Where the right was granted for an indefinite period, the resulting entity shall test the right for impairment at least annually, and whenever there is an indication that the right may be impaired. An acquirer that subsequently sells a reacquired right to a third party shall include the carrying amount of the intangible asset in determining the gain or loss on the sale.

*Transfers, Concessionary Loans and Similar Benefits Received by an Acquirer or Acquired Operation on the Basis of Criteria that may Change as a Result of an Acquisition*

114. A transfer, concessionary loan or similar benefit, previously received by an acquirer or an acquired operation on the basis of criteria that change as a result of an acquisition, shall be reassessed prospectively in accordance with other PBE Standards (paragraphs AG109–AG111 provide related application guidance).

*Contingent Liabilities*

115. After initial recognition and until the liability is settled, cancelled or expires, the acquirer shall measure a contingent liability recognised in an acquisition at the higher of:
- (a) The amount that would be recognised in accordance with PBE IPSAS 19; and
  - (b) The amount initially recognised less, if appropriate, cumulative amortisation recognised in accordance with PBE IPSAS 9 *Revenue from Exchange Transactions*.

This requirement does not apply to contracts accounted for in accordance with PBE IPSAS 29<sup>8</sup>.

*Indemnification Assets*

116. At the end of each subsequent reporting period, the acquirer shall measure an indemnification asset that was recognised at the acquisition date on the same basis as the indemnified liability or asset, subject to any contractual limitations on its amount and, for an indemnification asset that is not subsequently measured at its fair value, management's assessment of the collectibility of the indemnification asset. The acquirer shall derecognise the indemnification asset only when it collects the asset, sells it or otherwise loses the right to it.

*Contingent Consideration*

117. Some changes in the fair value of contingent consideration that the acquirer recognises after the acquisition date may be the result of additional information that the acquirer obtained after that date about facts and circumstances that existed at the acquisition date. Such changes are measurement period adjustments in accordance with paragraphs 103–107. However, changes resulting from events after the acquisition date, such as meeting an earnings target, reaching a specified share price or reaching a milestone on a research and development project, are not measurement period adjustments. The acquirer shall account for changes in the fair value of contingent consideration that are not measurement period adjustments as follows:
- (a) Contingent consideration classified as a component of net assets/equity shall not be remeasured and its subsequent settlement shall be accounted for within net assets/equity.
  - (b) Other contingent consideration that:
    - (i) Is within the scope of PBE IPSAS 29<sup>9</sup> shall be measured at fair value at each reporting date and changes in fair value shall be recognised in surplus or deficit in accordance with PBE IPSAS 29.
    - (ii) Is not within the scope of PBE IPSAS 29 shall be measured at fair value at each reporting date and changes in fair value shall be recognised in surplus or deficit.

<sup>8</sup> If an entity applies this Standard and early adopts PBE IFRS 9 *Financial Instruments*, the references to PBE IPSAS 29 in this paragraph shall be read as a reference to PBE IFRS 9.

<sup>9</sup> If an entity applies this Standard and early adopts PBE IFRS 9 *Financial Instruments*, the references to PBE IPSAS 29 in this paragraph shall be read as a reference to PBE IFRS 9.

*Income Taxes (where not Included in the Terms of the Acquisition)*

118. Acquisitions involving ~~public benefit public sector~~ entities in the public sector may result in a tax authority forgiving amounts of tax subsequent to the acquisition. The acquirer shall account for the tax forgiven prospectively in accordance with PBE IAS 12 ~~the relevant international or national accounting standard dealing with income taxes.~~

All the RDR concessions and RDR paragraphs are consistent with the proposed amendments for NZ IFRS 3 in the ED NZASB 2017-1 *Amendments to RDR for Tier 2 For-profit Entities*.

**Disclosures**

- \*119. The acquirer shall disclose information that enables users of its financial statements to evaluate the nature and financial effect of an acquisition that occurs either:**

- (a) **During the current reporting period; or**
- (b) **After the end of the reporting period but before the financial statements are authorised for issue.**

120. To meet the objective in paragraph 119, the acquirer shall disclose the following information for each acquisition that occurs during the reporting period:

- (a) The name and a description of the acquired operation.
- (b) The acquisition date.
- (c) The percentage of voting equity interests or equivalent acquired.
- \*(d) The primary reasons for the acquisition and a description of how the acquirer obtained control of the acquired operation including, where applicable, the legal basis for the acquisition.
- \*(e) A qualitative description of the factors that make up the goodwill recognised, such as expected synergies from combining the operations of the acquired operation and the acquirer, intangible assets that do not qualify for separate recognition or other factors.
- \*(f) The acquisition-date fair value of the total consideration transferred and the acquisition-date fair value of each major class of consideration, such as:
  - (i) Cash;
  - (ii) Other tangible or intangible assets, including an operation or controlled entity of the acquirer;
  - (iii) Liabilities incurred, for example, a liability for contingent consideration; and
  - (iv) Equity interests of the acquirer, including the number of instruments or interests issued or issuable and the method of measuring the fair value of those instruments or interests.
- (g) For contingent consideration arrangements and indemnification assets:
  - (i) The amount recognised as of the acquisition date;
  - (ii) A description of the arrangement and the basis for determining the amount of the payment; and
  - \*(iii) An estimate of the range of outcomes (undiscounted) or, if a range cannot be estimated, that fact and the reasons why a range cannot be estimated. If the maximum amount of the payment is unlimited, the acquirer shall disclose that fact.
- \*(h) For acquired receivables:
  - (i) The fair value of the receivables;
  - (ii) The gross amounts receivable in accordance with a binding arrangement; and
  - (iii) The best estimate at the acquisition date of the cash flows in accordance with a binding arrangement not expected to be collected.

The disclosures shall be provided by major class of receivable, such as loans, direct finance leases and any other class of receivables.



- (i) The amounts recognised as of the acquisition date for each major class of assets acquired and liabilities assumed.
- (j) For each contingent liability recognised in accordance with paragraph 77, the information required in paragraph 98 of PBE IPSAS 19. If a contingent liability is not recognised because its fair value cannot be measured reliably, the acquirer shall disclose:
  - (i) The information required by paragraph 100 of PBE IPSAS 19; and
  - (ii) The reasons why the liability cannot be measured reliably.
- \*(k) The total amount of goodwill that is expected to be deductible for tax purposes.
- \*(l) For transactions that are recognised separately from the acquisition of assets and assumption of liabilities in the acquisition in accordance with paragraph 109:
  - (i) A description of each transaction;
  - (ii) How the acquirer accounted for each transaction;
  - (iii) The amounts recognised for each transaction and the line item in the financial statements in which each amount is recognised; and
  - (iv) If the transaction is the effective settlement of a pre-existing relationship, the method used to determine the settlement amount.
- \*(m) The disclosure of separately recognised transactions required by (l) shall include the amount of acquisition-related costs and, separately, the amount of those costs recognised as an expense and the line item or items in the statement of ~~financial performance~~ comprehensive revenue and expense in which those expenses are recognised. The amount of any issue costs not recognised as an expense and how they were recognised shall also be disclosed.
- \*(n) In an acquisition in which a loss is recognised in surplus or deficit (see paragraph 86):
  - (i) The amount of the loss recognised in accordance with paragraph 86 and the line item in the statement of ~~financial performance~~ comprehensive revenue and expense in which the loss is recognised; and
  - (ii) A description of the reasons why the transaction resulted in a loss.

Agenda item 7.1 reference: RDR for acquisitions (paras 28–29).  
 Applied the Draft *Policy for Determining RDR for Tier 2 Entities in Australia and Tier 2 Entities For-Profit Entities in New Zealand* to paragraph 120(n). This is a public sector specific disclosure added by the IPSASB.

- \*(o) In a bargain purchase (see paragraphs 88–90):
  - (i) The amount of any gain recognised in accordance with paragraph 88 and the line item in the ~~statement of financial performance~~ statement of comprehensive revenue and expense in which the gain is recognised; and
  - (ii) A description of the reasons why the transaction resulted in a gain.
- \*(p) For each acquisition in which the acquirer holds less than 100 percent of the ~~equity quantifiable ownership~~ interests or equivalent in the acquired operation at the acquisition date:
  - (i) The amount of the non-controlling interest in the acquired operation recognised at the acquisition date and the measurement basis for that amount; and
  - (ii) For each non-controlling interest in an acquired operation measured at fair value, the valuation technique(s) and significant inputs used to measure that value.
- \*(q) In an acquisition achieved in stages:
  - (i) The acquisition-date fair value of the equity interest in the acquired operation held by the acquirer immediately before the acquisition date; and
  - (ii) The amount of any gain or loss recognised as a result of remeasuring to fair value the equity interest in the acquired operation held by the acquirer before the acquisition (see

paragraph 100) and the line item in the ~~statement of financial performance~~ statement of comprehensive revenue and expense in which that gain or loss is recognised.

\*(r) The following information:

- (i) The amounts of revenue and expense, and the surplus or deficit of the acquired operation since the acquisition date included in the consolidated ~~statement of financial performance~~ statement of comprehensive revenue and expense for the reporting period; and
- (ii) The revenue and expense, and the surplus or deficit of the combined entity for the current reporting period as though the acquisition date for all acquisitions that occurred during the year had been as of the beginning of the annual reporting period.

If disclosure of any of the information required by this subparagraph is impracticable, the acquirer shall disclose that fact and explain why the disclosure is impracticable. This Standard uses the term 'impracticable' with the same meaning as in PBE IPSAS 3.

RDR 120.1 A Tier-2 acquirer shall disclose the following information for each acquisition that occurs during the reporting period:

- (a) The acquisition-date fair value of the total consideration transferred;
- (b) The amount of the loss recognised in accordance with paragraph 86; and
- ~~(b)~~(c) In a bargain purchase (see paragraphs 88–90) the amount of any gain recognised in accordance with paragraph 88.

\*121. For individually immaterial acquisitions occurring during the reporting period that are material collectively, the acquirer shall disclose in aggregate the information required by paragraph 120(e)–(r).

RDR 121.1 For individually immaterial acquisitions occurring during the reporting period that are material collectively, a Tier 2 acquirer shall disclose in aggregate the information required by paragraphs 120(g)(i) and (ii), 120(i), 120(j) and RDR 120.1.

\*122. If the acquisition date of an acquisition is after the end of the reporting period but before the financial statements are authorised for issue, the acquirer shall disclose the information required by paragraph 120 unless the initial accounting for the acquisition is incomplete at the time the financial statements are authorised for issue. In that situation, the acquirer shall describe which disclosures could not be made and the reasons why they cannot be made.

\*123. **The acquirer shall disclose information that enables users of its financial statements to evaluate the financial effects of adjustments recognised in the current reporting period that relate to acquisitions that occurred in the period or previous reporting periods.**

\*124. To meet the objective in paragraph 123, the acquirer shall disclose the following information for each material acquisition or in the aggregate for individually immaterial acquisitions that are material collectively:

- (a) If the initial accounting for an acquisition is incomplete (see paragraph 103) for particular assets, liabilities, non-controlling interests or items of consideration and the amounts recognised in the financial statements for the acquisition thus have been determined only provisionally:
  - (i) The reasons why the initial accounting for the acquisition is incomplete;
  - (ii) The assets, liabilities, ~~equity quantifiable ownership~~ interests (or equivalent) or items of consideration for which the initial accounting is incomplete; and
  - (iii) The nature and amount of any measurement period adjustments recognised during the reporting period in accordance with paragraph 107.
- (b) For each reporting period after the acquisition date until the entity collects, sells or otherwise loses the right to a contingent consideration asset, or until the entity settles a contingent consideration liability or the liability is cancelled or expires:
  - (i) Any changes in the recognised amounts, including any differences arising upon settlement;
  - (ii) Any changes in the range of outcomes (undiscounted) and the reasons for those changes; and
  - (iii) The valuation techniques and key model inputs used to measure contingent consideration.



- (c) For contingent liabilities recognised in an acquisition, the acquirer shall disclose the information required by paragraphs 97 and 98 of PBE IPSAS 19 for each class of provision.
  - (d) A reconciliation of the carrying amount of goodwill at the beginning and end of the reporting period showing separately:
    - (i) The gross amount and accumulated impairment losses at the beginning of the reporting period.
    - (ii) Additional goodwill recognised during the reporting period, except goodwill included in a disposal group that, on acquisition, meets the criteria to be classified as held for sale in accordance with PBE IFRS 5.
    - (iii) Adjustments resulting from the subsequent recognition of amounts during the reporting period in accordance with PBE IAS 12~~the relevant international or national accounting standard dealing with income taxes.~~
    - (iv) Goodwill included in a disposal group classified as held for sale in accordance with PBE IFRS 5 and Goodwill derecognised during the reporting period without having previously been included in a disposal group classified as held for sale.
    - (v) Impairment losses recognised during the reporting period in accordance with PBE IPSAS 26 *Impairment of Cash-Generating Assets*. (PBE IPSAS 26 requires disclosure of information about the recoverable amount and impairment of goodwill in addition to this requirement.)
    - (vi) Net exchange rate differences arising during the reporting period in accordance with PBE IPSAS 4 *The Effects of Changes in Foreign Exchange Rates*.
    - (vii) Any other changes in the carrying amount during the reporting period.
    - (viii) The gross amount and accumulated impairment losses at the end of the reporting period.
  - (e) The amount and an explanation of any gain or loss recognised in the current reporting period that both:
    - (i) Relates to the identifiable assets acquired or liabilities assumed in an acquisition that was effected in the current or previous reporting period; and
    - (ii) Is of such a size, nature or incidence that disclosure is relevant to understanding the combined entity's financial statements.
- And
- (f) If amounts of tax due are forgiven as a result of the terms of the acquisition (see paragraphs 78–79):
    - (i) The amount of tax due that was forgiven; and
    - (ii) Where the acquirer is the tax authority, details of the adjustment made to tax receivable.

Agenda item 7.1 reference: RDR for acquisitions (paras 28–29).  
 Paragraph 124(f) is a public sector specific disclosure added by the IPSASB. We applied the Draft *Policy for Determining RDR for Tier 2 Entities in Australia and Tier 2 Entities For-Profit Entities in New Zealand* to paragraph 124(f) and propose no RDR concession.

RDR 124.1 A Tier 2 acquirer shall disclose the following information for each material acquisition or in the aggregate for individually immaterial acquisitions that are material collectively:

- (a) For contingent liabilities recognised in an acquisition, the information required by paragraph 98 of PBE IPSAS 19 for each class of provision;
- (b) Impairment losses on goodwill recognised during the reporting period in accordance with PBE IPSAS 26. (PBE IPSAS 26 requires disclosure of information about the recoverable amount and impairment of goodwill in addition to this requirement.); and
- (c) If amounts of tax due are forgiven as a result of the terms of the acquisition (see paragraphs 78):
  - (i) The amount of tax due that was forgiven; and
  - (ii) Where the acquirer is the tax authority, details of the adjustment made to tax receivable.

- \*125. If the specific disclosures required by this and other PBE Standards do not meet the objectives set out in paragraphs 119 and 123, the acquirer shall disclose whatever additional information is necessary to meet those objectives.

**RDR 125.1 A Tier 2 entity is required to comply with the disclosures in paragraphs 120–124 that are not asterisked (\*) as RDR concessions.**

Agenda item 7.1 reference: RDR for acquisitions (paras 28–29).
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## Effective Date and Transition

### Effective Date

126. ~~[Not used] This Standard shall be applied prospectively to public sector combinations for which the amalgamation date or acquisition date is on or after the beginning of the first annual reporting period beginning on or after January 1, 2019. Earlier application is encouraged. If an entity applies this Standard before January 1, 2019, it shall disclose that fact.~~

**126.1 A public benefit entity shall apply this Standard for annual financial statements covering periods beginning on or after [date]. Earlier application is permitted. If a public benefit entity applies this Standard for a period beginning before [date], it shall disclose that fact.**

### Transition

127. Assets and liabilities that arose from ~~PBE~~~~public sector~~ combinations whose acquisition dates or amalgamation dates preceded the application of this Standard shall not be adjusted upon application of this Standard.
128. Contingent consideration balances arising from acquisitions whose acquisition dates preceded the date when an entity first applied this Standard shall not be adjusted upon first application of this Standard. Paragraphs 129–132 shall be applied in the subsequent accounting for those balances. Paragraphs 129–132 shall not apply to the accounting for contingent consideration balances arising from acquisitions with acquisition dates on or after the date when the entity first applied this Standard. In paragraphs 129–132 acquisitions refers exclusively to acquisitions whose acquisition date preceded the application of this Standard.
129. If an acquisition agreement provides for an adjustment to the cost of the acquisition contingent on future events, the acquirer shall include the amount of that adjustment in the cost of the acquisition at the acquisition date if the adjustment is probable and can be measured reliably.
130. An acquisition agreement may allow for adjustments to the cost of the acquisition that are contingent on one or more future events. The adjustment might, for example, be contingent on a specified level of profit being maintained or achieved in future periods, or on the market price of the instruments issued being maintained. It is usually possible to estimate the amount of any such adjustment at the time of initially accounting for the acquisition without impairing the reliability of the information, even though some uncertainty exists. If the future events do not occur or the estimate needs to be revised, the cost of the acquisition shall be adjusted accordingly.
131. However, when an acquisition agreement provides for such an adjustment, that adjustment is not included in the cost of the acquisition at the time of initially accounting for the acquisition if it either is not probable or cannot be measured reliably. If that adjustment subsequently becomes probable and can be measured reliably, the additional consideration shall be treated as an adjustment to the cost of the acquisition.
132. In some circumstances, the acquirer may be required to make a subsequent payment to the seller as compensation for a reduction in the value of the assets given, equity instruments issued or liabilities incurred or assumed by the acquirer in exchange for control of the acquired operation. This is the case, for example, when the acquirer guarantees the market price of equity or debt instruments issued as part of the cost of the acquisition and is required to issue additional equity or debt instruments to restore the originally determined cost. In such cases, no increase in the cost of the acquisition is recognised. In the case of equity instruments, the fair value of the additional payment is offset by an equal reduction in the value attributed to the instruments initially issued. In the case of debt instruments, the additional payment is regarded as a reduction in the premium or an increase in the discount on the initial issue.

133. An entity, such as a mutual entity, that has not yet applied this Standard and had one or more ~~PBE public sector~~ combinations that were accounted for using the purchase method (which involves the amortisation of goodwill) shall apply the transition provisions in paragraphs AG114–AG115.

#### *Income Taxes*

134. For ~~PBE public sector~~ combinations in which the acquisition date or amalgamation date was before this Standard is applied, the acquirer or resulting entity shall apply the requirements of ~~PBE IAS 12 the relevant international or national accounting standard dealing with income taxes~~ prospectively. From the date when this Standard is applied, the acquirer or resulting entity shall recognise any changes required by ~~PBE IAS 12 the relevant international or national accounting standard dealing with income taxes~~ as an adjustment to surplus or deficit (or, if required by ~~PBE IAS 12 the relevant international or national accounting standard dealing with income taxes~~, outside surplus or deficit).

### **Withdrawal and Replacement of PBE IFRS 3 (2014)**

- 134.1 This Standard supersedes PBE IFRS 3 (2014). PBE IFRS 3 remains applicable until PBE IPSAS 40 is applied or becomes effective, whichever is earlier.

## Application Guidance

*This Appendix is an integral part of PBE IPSAS 40*

### Definitions (see paragraph 5)

- AG1. Paragraph 5 of this Standard defines a resulting entity as “the entity that is the result of two or more operations combining in an amalgamation.” ~~A resulting entity is not initially a party to the public sector combination. A resulting entity may have the legal form of a new entity, or may retain the legal identity of one of the combining operations. However, a resulting entity usually has the economic substance of a new entity. In a combination in which one party to the combination gains control of one or more operations, and in which the economic substance is that of an amalgamation, the nature of the combination is usually that the resulting entity has the substance of a new entity.~~

### Identifying a PBE-public sector Combination (see paragraph 6)

- AG2. Paragraph 5 of this Standard defines a PBE-public sector combination as “the bringing together of separate operations into one PBE-public sector entity.” The reference to one PBE-public sector entity may be to a single entity or to an economic entity. Some public benefit entity sector reorganizations may involve more than one entitypublic sector combination. The circumstances in which a PBE-public sector combination might occur include:

- (a) By mutual agreement; and
- (b) By compulsion (for example by legislation).

- AG3. Paragraph 5 of this Standard defines an operation as “an integrated set of activities and related assets and/or liabilities that is capable of being conducted and managed for the purpose of achieving an entity’s objectives, by providing goods and/or services.”

- AG4. An operation consists of inputs and processes applied to those inputs that have the ability to create outputs. Although operations usually have outputs, outputs are not required for an integrated set of activities and related assets and/or liabilities to qualify as an operation. For the purposes of this standard, the three elements of an operation are defined as follows:

- (a) **Input:** Any economic resource that creates, or has the ability to create, outputs when one or more processes are applied to it.
- (b) **Process:** Any system, standard, protocol, convention or rule that when applied to an input or inputs, creates or has the ability to create outputs.
- (c) **Output:** The result of inputs and processes applied to those inputs that provide, or have the ability to provide a return in the form of dividends, lower costs or other economic benefits directly to investors or other owners, members or participants. Outputs may also be in the form of goods and services for community or social benefit, goods and/or services.

~~The definitions of an input and an output differ from those in RPG 3, Reporting Service Performance Information. This is because RPG 3 focuses on recipients who are external to the entity; an operation may have recipients who are internal to an entity.~~

Agenda item 7.1 reference: Examples of the components of an operation (paras 32–33).

- AG5. To be capable of being conducted and managed for the purposes defined, an integrated set of activities and assets and/or liabilities requires two essential elements—inputs and processes applied to those inputs, which together are or will be used to create outputs. However, an operation need not include all of the inputs or processes that the transferor used in operating that operation if the entity that receives the operation or operations is capable of continuing to produce outputs, for example, by integrating the operation with their own inputs and processes.
- AG6. The nature of the elements of an operation varies by sector and by the structure of an entity’s operations (activities), including the entity’s stage of development. Established operations often have many different types of inputs, processes and outputs, whereas new operations often have few inputs and processes and sometimes only a single output (product). Nearly all operations also have liabilities, but an operation need not have liabilities.

- AG7. An integrated set of activities and assets and/or liabilities in the development stage might not have outputs. In these cases, the entity that receives the operation should consider other factors to determine whether the set is an operation. Those factors include, but are not limited to, whether the set:
- (a) Has begun planned principal activities;
  - (b) Has employees, intellectual property and other inputs and processes that could be applied to those inputs;
  - (c) Is pursuing a plan to produce outputs; and
  - (d) Will be able to obtain access to service recipients that will receive the outputs.
- Not all of those factors need to be present for a particular integrated set of activities and assets and/or liabilities in the development stage to qualify as an operation.
- AG8. Determining whether a particular set of activities and assets and/or liabilities is an operation should be based on whether the integrated set is capable of being conducted and managed as an operation by another entity. Thus, in evaluating whether a particular set is an operation, it is not relevant whether a transferor operated the set as an operation or whether the acquirer intends to operate the set as an operation.
- AG9. In the absence of evidence to the contrary, a particular set of activities and assets and/or liabilities in which goodwill is present shall be presumed to be an operation. However, an operation need not have goodwill.

#### Classification of ~~PBE public sector~~ Combinations (see paragraphs 7–14)

##### *Assessment of Control (see paragraphs 7–8)*

- AG10. Where a party to a ~~PBE public sector~~ combination gain controls of one or more operations as a result of that combination, the combination is classified as either an amalgamation or an acquisition, depending on the economic substance of the combination. If no party to the combination gains control, the combination is classified as an amalgamation. In making this assessment the first step is to determine whether one of the entities that existed prior to the ~~PBE public sector~~ combination has gained control of one or more operations. Because this determination is made by reference to the entities that existed prior to the ~~PBE public sector~~ combination, it differs from the assessment of control made in accordance with PBE IPSAS 35 *Consolidated Financial Statements*<sup>10</sup>, where the assessment of control is made by reference to the entities that exist after a ~~PBE public sector~~ combination has taken place.
- AG11. In determining whether one party to a ~~PBE public sector~~ combination gains control of one or more operations as a result of the combination, an entity applies the principles and guidance in PBE IPSAS 35. In applying the principles and guidance, references to “an entity controls” are read as “an entity gains control of” and references to “another entity” are read as “an operation”. For example, in determining whether one party to a ~~PBE public sector~~ combination gains control of one or more operations as a result of the combination for the purposes of this Standard, paragraph 20 of PBE IPSAS 35 should be read as follows (amended text is shown in *italics*):

Thus, an entity *gains control of an operation* if and only if the entity *gains* all the following:

- (a) Power over the operation (see paragraphs 23–29);
- (b) Exposure, or rights, to variable benefits from its involvement with the operation (see paragraphs 30–34); and
- (c) The ability to use its power over the operation to affect the nature or amount of the benefits from its involvement with the operation (see paragraphs 35–37).

- AG12. In applying the principles and guidance in PBE IPSAS 35, an entity has regard to paragraphs AG13–AG18.

<sup>10</sup> If an entity applies this Standard before it applies PBE IPSAS 35 *Consolidated Financial Statements*, any reference to PBE IPSAS 35 shall be read as references to PBE IPSAS 6 *Consolidated and Separate Financial Statements* (PS) or PBE IPSAS 6 *Consolidated and Separate Financial Statements* (NFP).

- AG13. A ~~PBE-public-sector~~ combination effected primarily by the transfer of consideration (i.e., by transferring cash or other assets or by incurring liabilities) usually results in one entity gaining control of one or more operations.
- AG14. A ~~PBE-public-sector~~ combination effected primarily by exchanging equity interests usually results in one entity gaining control of one or more operations. Combinations involving an exchange of equity interests usually results in one entity having sufficient voting rights to gain control of one or more operations. This may occur without the entity having a majority of the voting rights where the entity has a large minority voting interest and no other owner or organised group of owners has a significant voting interest.
- AG15. A ~~PBE-public-sector~~ combination involving the issuance of equity interests may give rise to a reverse acquisition (see paragraphs AG66–AG71). An entity considers this possibility in determining whether one party to a ~~PBE-public-sector~~ combination gains control of operations.
- AG16. In a ~~PBE-public-sector~~ combination involving more than two entities, the party to the ~~PBE-public-sector~~ combination that initiates the combination (if any) is more likely to gain control of operations than the other parties to the combination.
- AG17. In a ~~PBE-public-sector~~ combination in which a new legal entity is formed to effect the combination, that entity may gain control of operations only where the entity exists prior to the combination taking place. Where this new legal entity does not exist prior to the combination taking place, an entity considers whether one of the parties to the combination that existed prior to the combination taking place gains control of operations.
- AG18. If the application of this guidance identifies one party to the combination as gaining control of one or more operations, the combination is classified as either an amalgamation or an acquisition, depending on the economic substance of the combination. An entity considers the guidance in paragraphs 9–14 and AG19–AG50 to determine whether the economic substance of the combination is that of an amalgamation. If the application of the guidance does not identify one party to the combination as gaining control of one or more operations, the combination shall be classified as an amalgamation.

*Assessment of the Classification of a-~~PBEpublic-sector~~ Combination (see paragraphs 9–14)*

- AG19. If one party to a ~~PBE-public-sector~~ combination gains control of one or more operations as a result of the combination, the combination shall be classified as either an amalgamation or an acquisition, depending on the economic substance of the combination. In assessing whether the economic substance of the combination is that of an amalgamation, an entity considers the economic substance of the ~~PBEpublic-sector~~ combination and the indicators in paragraphs 12–14. A combination that does not have the economic substance of an amalgamation shall be classified as an acquisition. In making this assessment, an entity considers the following guidance.

*Economic Substance (see paragraph 9)*

- AG20. Usually, an analysis of the indicators in paragraphs 12–13, individually or on combination, will produce a conclusive result and provide sufficient evidence to determine whether the economic substance of the combination is that of an amalgamation. A combination does not need to satisfy both of these indicators to be classified as an amalgamation.
- AG21. Where consideration of the indicators in paragraphs 12–13 produces inconclusive results or does not provide sufficient evidence to clearly determine the economic substance of the combination, an entity considers the additional matters in paragraph 14.
- AG22. As noted in paragraph AG1, the resulting entity following an amalgamation usually has the economic substance of a new entity regardless of whether it has been established as a new legal entity. The economic substance of an amalgamation is usually that a new entity is formed, irrespective of the legal form of the resulting entity. This applies equally to a combination in which one party to the combination gains control of one or more operations. If the economic substance of a ~~PBE-public-sector~~ combination is that one of the parties to the combination continues to exist, this may provide evidence that the economic substance of the combination is that of an acquisition; however, —In combinations of operations under common control, the fact that the ultimate controlling entity controls the operations both before and after the combination reduces the significance of this factor.



AG23. An amalgamation involves the integration of the operations that are part of the ~~PBE public sector~~ combination. ~~Generally in other words~~, an amalgamation does not give rise to a controlling entity/controlled entity relationship between parties to a combination. If, following the combination, any of the operations operate as controlled entities of a party to the combination, this may provide evidence that the economic substance of the combination is that of an acquisition. However, there could be circumstances where a controlling entity/controlled entity relationship between parties to a combination remains after the combination. For example, there could be legal, tax or administrative reasons for leaving the existing operations of the combining entities within their respective existing legal entity structure, which could entail establishing a controlled entity/controlling entity structure as part of the combination, but that outcome does not necessarily mean that the economic substance of the combination is an acquisition.

AG24. An acquisition is usually a mutual agreement between two or more parties, and usually has commercial substance. However, it is possible for an acquisition to occur without mutual agreement (for example, a forced nationalisation) in the public sector, a party to the combination may be able to impose a public sector combination on the other party to the combination. Where this results in the entity gaining access to economic benefits or service potential that are similar to those that could have been obtained by mutual agreement, it is probable that the economic substance of the public sector combination is that of an acquisition. For example, a central government may centralize a service for which it had been providing funding, by requiring local government entities to transfer operations to the central government in order to achieve economies of scale. Where the entity does not gain access to economic benefits or service potential that are similar to those that could have been obtained in a voluntary transaction, it is probable that the economic substance of the public sector combination is that of an amalgamation.

Agenda item 7.1 reference: Benefits obtained by mutual agreement (paragraph AG24) (paras 30–31).
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AG25. Where, after consideration of the indicators and the nature of the ~~PBE public sector~~ combination, there is insufficient evidence that the ~~PBE public sector~~ combination has the economic substance of an amalgamation, the combination shall be classified as an acquisition.

Indicators Relating to Consideration (see paragraph 12)

AG26. Amalgamations usually do not involve the payment of consideration to compensate a seller for giving up their entitlements to the net assets of an operation. By contrast, acquisitions usually involve an exchange of consideration between those gaining control of the operations and those losing control of the operations.

AG27. The payment of consideration that is intended to compensate those with an entitlement to the net assets of the transferred operation for giving up that entitlement provides evidence that the economic substance of the ~~PBE public sector~~ combination is an acquisition. In such cases, the combination is classified as an acquisition.

AG28. The payment of consideration that is not intended to compensate the seller for giving up their entitlements to the net assets of an operation, but is, for example, intended to reimburse them for costs incurred in effecting the ~~PBE public sector~~ combination, may provide evidence that the economic substance of the combination is that of an amalgamation.

AG29. Acquisitions may occur without an exchange of consideration, for example where an individual bequeaths an operation to a government entity. Consequently, the absence of consideration does not in itself provide evidence of the economic substance of the ~~PBE public sector~~ combination. In assessing consideration, an entity also considers the reasons why consideration was either paid or not paid.

AG30. Where a ~~PBE public sector~~ combination does not include the payment of consideration, an entity considers the reasons why no consideration has been paid. If the former owner has given up their entitlements to the net assets of an operation, or has had their entitlements extinguished through compulsion (for example, in an uncompensated seizure), there may be evidence that the combination is an acquisition.

AG31. ~~[Not used] Where a public sector combination does not include the payment of consideration because there is no party with an entitlement to the net assets of an operation, the economic substance of the combination will usually be that of an amalgamation. An acquisition involves a transfer of an operation from its former owner to its new owner. If there is no party with an entitlement to the net assets of an~~

~~operation, there is no former owner, and the combination is usually not an acquisition. This scenario will only arise where a complete entity is being transferred; where an individual operation is being transferred, the entity transferring the operation will be the former owner and will be entitled to the net assets of the operation. Examples of entities where there will be no former owner(s) include municipalities and some not for profit organisations.~~

Indicators Relating to the Decision-Making Process (see paragraph 13)

- AG32. An acquisition usually requires the voluntary participation of all the parties to the combination. Consequently, where a ~~PBE-public sector~~ combination is imposed by a third party without any party to the combination being involved in the decision-making process, this may provide evidence that the economic substance of the combination is an amalgamation.
- AG33. In other circumstances, the parties to the ~~PBEpublic sector~~ combination will be able to influence the terms of the combination to different degrees even when the combination is imposed by a third party. As the degree of influence the parties to the combination have increases, particularly the influence of the party that gains control of one or more operations, it becomes less likely that a conclusion regarding the economic substance of the combination can be drawn.
- AG34. For example, the parties to the combination may be directed to combine by a regulator, but the regulator allows the parties to determine the terms of the combination. The economic substance of this ~~PBEpublic sector~~ combination is likely to be determined by the terms of the combination agreed by the parties rather than by the decision of the regulator that the parties must combine.
- AG35. Where the party to the ~~PBEpublic sector~~ combination that gains control of one or more operations is able to impose the combination on the other party, this does not provide evidence that the economic substance of the combination is that of an amalgamation. For example, a government may decide to nationalise a private sector entity, contrary to the wishes of the shareholders. The fact that the government (a party to the combination) is able to impose the nationalisation, for example through legislation, does not provide evidence that the economic substance of the combination is an amalgamation. Where the party to the combination that gains control of one or more operations is able to impose the combination on the other party, this provides evidence that the economic substance of the combination is that of an acquisition.
- AG36. Where a ~~PBE-public sector~~ combination is subject to approval by each party's citizens through referenda, this may provide evidence that the economic substance of the combination is that of an amalgamation. Such a requirement provides evidence that the parties to the combination do not have freedom to voluntarily effect the combination and that the ultimate decision as to whether the combination takes place is taken by third parties. However, it is possible for citizens to approve, through referenda, a combination whose terms are those of an acquisition.
- AG37. Where a ~~PBE-public sector~~ combination takes place between two parties that are under common control, this may provide evidence that the economic substance of the combination is that of an amalgamation. ~~PBEPublic sector~~ combinations under common control are often instigated by and on behalf of the controlling entity, and the controlling entity will often determine the terms of the combination. For example, a government may decide to combine two ministries for administrative or political reasons, and specify the terms of the combination. In such circumstances, the ultimate decision as to whether the combination takes place, and the terms of the combination, are determined by the controlling entity. This provides evidence that the economic substance of the combination is an amalgamation.
- AG38. In some circumstances, two operations under common control may agree to combine voluntarily. However, this decision will usually be subject to the approval of the controlling entity, whether this approval is given explicitly or not. Where the approval of the controlling entity is required, this provides evidence that the ultimate decision as to whether the combination takes place, and the terms of the combination, are determined by the controlling entity. Consequently, this provides evidence that the economic substance of the combination is that of an amalgamation.

AG38.1 Despite the indicators in paragraph 13, a voluntary combination of two operations not under common control could be classified as an amalgamation. This type of combination is more frequent in the not-for-profit sector than the public sector. The two operations could combine to improve services to their recipients or to reduce operating cost. The two operations are uniting rather than one entity gains control of the other entity.



- AG39. Only where there is no evidence that the controlling entity is involved in the ~~PBEpublic-sector~~ combination, either by instigating the combination, determining the terms of the combination, or approving (whether explicitly or implicitly) the combination, will there be no evidence that the economic substance of the combination is that of an amalgamation. In such circumstances, the entity considers all other factors in determining the classification of the ~~PBEpublic-sector~~ combination.

Additional Matters to be Considered where the Indicators Relating to Consideration and the Decision-Making Process do not Provide Sufficient Evidence to Determine whether the Economic Substance of the Combination is that of an Amalgamation (see paragraph 14)

- AG40. Where an analysis of the indicators relating to consideration and the decision-making process produces inconclusive results or does not provide sufficient evidence to determine whether the economic substance of the combination is that of an amalgamation, an entity considers which classification and resulting accounting treatment would provide information that:
- (a) Best meets the objectives of financial reporting; and
  - (b) Best satisfies the qualitative characteristics (QCs).
- AG41. An analysis of the indicators relating to consideration and the decision-making process will usually produce a conclusive result and provide sufficient evidence to determine whether the economic substance of the combination is that of an amalgamation. This is because the indicators relating to consideration and the decision-making process will provide evidence of the economic substance of a ~~PBEpublic-sector~~ combination in all but exceptional circumstances. As a result, where it is clear that the indicators have been met, the additional matters set out in paragraph 14 are not considered in determining the classification.
- AG42. Where an analysis of the indicators relating to consideration and the decision-making process provides inconclusive results or does not provide sufficient evidence to determine whether the economic substance of the combination is that of an amalgamation, an entity considers which classification would provide information that best meets the objectives of financial reporting. The determination of whether a ~~PBEpublic-sector~~ combination is classified as an acquisition or an amalgamation can significantly affect the financial reporting of the combination. Consequently, it is important to consider the information each method provides and the principal users of that information.
- AG43. The modified pooling of interests method views the combination from the perspective of each of the combining entities and their owners or constituents who are uniting their interests in the resulting entity. Using the modified pooling of interests method of accounting, the combining operations measure the reported assets and liabilities at their carrying amounts in the financial statements of the combining operations as of the amalgamation date. Such information may assist users in assessing the performance of the resulting entity based upon the combined historical assets and liabilities of the combining operations at the date of the amalgamation and in comparing operating results with prior periods. However, this comparability may be reduced where adjustments to achieve consistent accounting policies are required. ~~It does not include information about the market's expectation of the value of the future cash flows associated with assets and liabilities, other than assets and liabilities recorded at fair value prior to the date of the amalgamation.~~
- AG44. The acquisition method views a combination from the perspective of the acquirer—the entity that gains control of the other operations. The acquirer purchases or otherwise gains control over net assets and recognises in its financial statements the assets acquired and liabilities assumed, including those not previously recognised by the acquired operation. Such information assists users of the financial statements in assessing the initial investments made, where paid, and the subsequent performance of those investments and comparing them with the performance of other entities based on the investment made by the acquirer. ~~It also includes information about the market's expectation of the value of the future cash flows associated with those assets and liabilities.~~ While it revalues the assets and liabilities of the acquired operation, it does not affect the valuation of assets and liabilities held by the acquirer prior to the acquisition. Further, depending on the relationship between the amounts in paragraph 85(a) and 85(b) and other factors (for example, a bargain purchase), it may result in the immediate recognition of a gain or loss through surplus or deficit.

<p>Agenda item 7.1 reference: Additional matters to be considered re indicators (paragraphs AG44 and AG45) (paras 37–38).</p>
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AG45. The information provided by each approach is summarised in the following table.

	<b>Amalgamation</b>	<b>Acquisition</b>
Perspective	Perspective of each of the combining operations and their owners or constituents.	Perspective of the acquirer.
User information	Assists users of the financial statements in assessing the performance of the resulting entity based upon the combined historical assets and liabilities of the combining operations at the date of the amalgamation and in comparing operating results with prior periods.	Assists users of the financial statements in assessing the initial investments made, <u>where paid</u> , and the subsequent performance of those investments.
Basis of reported values	Measures the reported assets and liabilities at their carrying amounts in the financial statements of the combining operations as of the amalgamation date.	Revalues the identifiable assets and liabilities of the acquired operation but does not affect the valuation of assets and liabilities held by the acquirer. <del>Includes information about the market's expectation of the value of the future cash flows associated with those assets and liabilities.</del>
Ability to compare to operating results of prior periods	May facilitate the comparison of operating results with prior periods. Comparability may be reduced where adjustments to achieve consistent accounting policies are required.	Difficult to compare operating results with prior periods.

- AG46. Consideration of which classification would provide information that best meets the objectives of financial reporting provides evidence of the economic substance of the ~~PBEpublic sector~~ combination where an analysis of the indicators relating to consideration and the decision-making process provides inconclusive results or does not provide sufficient evidence to determine whether the economic substance of the combination is that of an amalgamation.
- AG47. Where an analysis of the indicators relating to consideration and the decision-making process provides inconclusive results or does not provide sufficient evidence to determine the classification of the combination, an entity considers which classification would provide information that best satisfies the QCs of relevance, faithful representation, understandability, timeliness, comparability and verifiability. In making this assessment, an entity also considers the constraints on information included in general purpose financial reports, which are materiality, cost-benefit and the balance between the QCs.
- AG48. When considering the classification of a ~~PBEpublic sector~~ combination, some QCs will be more significant than others. For example, timeliness will be less significant than understandability when considering whether a combination is an amalgamation or an acquisition.
- AG49. An entity considers the QCs and the constraints on information from the perspective of the users of the financial statements. This will include consideration of the following questions; this list is not exhaustive.
- (a) Which classification most faithfully represents the economic substance of the ~~PBEpublic sector~~ combination, which may be different from its legal form? Does that classification faithfully represent an entity's financial performance and financial position?

- (b) Which classification will help users understand the nature of the ~~PBEpublic sector~~ combination? For example, in an amalgamation, any difference between the total recognised assets and total recognised liabilities is recognised in net assets/equity, whereas in an acquisition, the acquirer recognises goodwill, or a gain or loss in the reporting period. Which approach best helps the user to understand the nature of the combination?
- (c) Users' needs are best served when the information provided in respect of a transaction is comparable. How are similar ~~PBEpublic sector~~ combinations classified?

AG50. Consideration of which classification would provide information that best meets the QCs provides evidence of the economic substance of the ~~PBEpublic sector~~ combination where an analysis of the indicators relating to consideration and the decision-making process provides inconclusive results or does not provide sufficient evidence to determine whether the economic substance of the combination is that of an amalgamation.

### Accounting for Amalgamations

#### *Eliminating Transactions between the Combining Operations (see paragraph 22)*

- AG51. A resulting entity eliminates the effects of all transactions between the combining operations. For many transactions, elimination will take place automatically. For example, one combining operation provided services for a fee to another combining operation prior to the amalgamation date. The revenue of the combining operation that provided the services is reflected in that combining operation's ~~accumulated surplus or deficit~~accumulated comprehensive revenue and expense at the amalgamation date. The expense of the combining operation receiving the services is reflected in that combining operation's ~~accumulated surplus or deficit~~accumulated comprehensive revenue and expense at the amalgamation date. The resulting entity will recognise both amounts in net assets/equity.
- AG52. Elimination may not take place automatically where one combining operation has recognised an asset, and another combining operation has recognised a corresponding liability as a result of the transaction between two combining operations. The resulting entity eliminates both the asset and the liability, and recognises any difference between the asset and liability in net assets/equity.

#### *Carrying Amounts to be Used (see paragraphs 26–27)*

- AG53. Where a combining operation has previously been acquired in an acquisition (i.e., it was previously an acquired operation), the carrying amounts of the combining operation's assets and liabilities in its separate financial statements may be different to the carrying amounts of those assets and liabilities in the controlling entity's financial statements. In an acquisition, the controlling entity would measure the combining operation's assets and liabilities at their fair value. However, where the combining operation (i.e., the previously acquired operation) continues to prepare separate financial statements, it would use its previous carrying amounts. The fair value measurements in the financial statements of the controlling entity are not pushed down to the combining operation.
- AG54. To meet the requirements in paragraphs 26–27, a resulting entity measures the identifiable assets and liabilities of the combining operations at their carrying amounts in the financial statements of the combining operations as of the amalgamation date, subject to the requirement to adjust the carrying amounts to conform to the resulting entity's accounting policies. ~~The resulting entity does not measure the assets and liabilities at the carrying amounts in the financial statements of the controlling entity.~~

#### *Licences and Similar Rights Previously Granted by One Combining Operation to Another Combining Operation (see paragraph 32)*

- AG55. As part of an amalgamation, a resulting entity may receive a licence or similar right that had previously been granted by one combining operation to another combining operation to use one or more of the grantor's recognised or unrecognised assets. Examples of such rights include a right to use the acquirer's technology under a technology licencing agreement. The resulting entity recognises this licence or similar right as an identifiable intangible asset, and measures the intangible asset at its carrying amount in the financial statements of the combining operation as of the amalgamation date. Because the licence or similar right has previously been part of a binding arrangement, the licence satisfies both the separability and binding arrangement criteria in PBE IPSAS 31 *Intangible Assets*. Paragraph 47 provides guidance on the subsequent accounting for a licence or similar right previously granted by one combining operation to another combining operation.

- AG56. The resulting entity assesses both the licence or similar right previously granted by one combining operation to another combining operation, and the underlying asset (where the underlying asset is a recognised asset) for impairment in accordance with PBE IPSAS 21 *Impairment of Non-Cash-Generating Assets* and PBE IPSAS 26 *Impairment of Cash-Generating Assets*, at the amalgamation date.

*Forgiveness of Amounts of Tax Due in an Amalgamation (where Included in the Terms of the Amalgamation)*  
(see paragraphs 33–34)

- AG57. The resulting entity shall not recognise any amounts in respect of a combining operation's tax due where these amounts have been forgiven by a tax authority as part of the terms of the amalgamation. Where tax forgiveness occurs subsequent to an amalgamation, the resulting entity applies the requirements in paragraph 49. In applying the modified pooling of interests method of accounting, the resulting entity shall treat those amounts included in the terms of the amalgamation as having been derecognised prior to the amalgamation. The resulting entity shall account for a combining operation's tax due that has not been forgiven by a tax authority in accordance with PBE IAS 12~~the relevant international or national accounting standard dealing with income taxes.~~
- AG58. ~~[Not used] Where, as a result of the amalgamation, the resulting entity becomes the tax authority, it shall derecognise any tax receivable relating to the combining operation's tax due that has been forgiven in accordance with PBE IPSAS 23 Revenue from Non-Exchange Transactions (Taxes and Transfers).~~

Agenda item 7.1 reference: Tax forgiven (paras 22–27)
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*Recognition of Goodwill (see paragraph 36)*

- AG59. Amalgamations do not give rise to goodwill, and consequently a resulting entity does not recognise goodwill arising from an amalgamation. Paragraphs 37–38 specify the treatment of the net assets/equity arising as a result of the amalgamation.
- AG60. Where a combining operation has previously recognised goodwill as a result of a previous acquisition, the resulting entity recognises this goodwill in its opening statement of financial position.

*Subsequent Measurement of Transfers, Concessionary Loans and Similar Benefits Received by a Combining Operation on the Basis of Criteria that may Change as a Result of an Amalgamation (see paragraph 48)*

- AG61. Prior to an amalgamation taking place, a combining operation may receive a transfer from a third party, based on specified criteria. For example, a national government may provide grants to those municipalities where the average household income is below a threshold. An amalgamation of two municipalities may involve one municipality which met the criteria and received the grant, and one municipality which did not meet the criteria and which did not receive the grant. Following the amalgamation, the average household income of the new, combined municipality will either be above or below the threshold, which may cause the grantor to reassess the amount of grant given.
- AG62. The resulting entity shall not account for any revisions to the grant amount as part of the amalgamation, but shall account for any revisions at the point the grantor makes its intentions known in accordance with other PBE Standards.
- AG63. Similar circumstances may arise in respect of concessionary loans and other benefits. The resulting entity shall not account for any revisions to those transactions as part of the amalgamation, but shall account for any revisions at the point the grantor makes its intentions known in accordance with other PBE Standards.

*Amalgamations Occurring During a Reporting Period (see paragraphs 50–52)*

- AG64. To meet the requirements of paragraphs 50–52, the resulting entity is not required to present financial statements for periods prior to the amalgamation date, although it may elect to do so by making the disclosures specified in paragraph 54(g). Where the resulting entity does not elect to present financial statements for periods prior to the amalgamation date, it meets the needs of the users of its financial statements for information about the combining operations prior to the amalgamation by:
- (a) Where financial statements have been issued on behalf of the combining operations for a reporting period ending immediately prior to the amalgamation date (which may be a partial

period), directing the users of its financial statements to the financial statements issued on behalf of the combining operations.

- (b) Where no financial statements have been issued on behalf of the combining operations for a reporting period ending immediately prior to the amalgamation date (which may be a partial period), making the disclosures required by paragraph 54(h).

AG65. ~~[Not used] To satisfy the requirements of a regulator, it may be necessary for the combining operations and/or the resulting entity to present or disclose information in addition to that required by this Standard.~~

## Accounting for Acquisitions

### *Reverse Acquisitions*

AG66. A reverse acquisition occurs when the entity that issues securities (the legal acquirer) is identified as the acquired operation for accounting purposes on the basis of the guidance in paragraphs AG10–AG18. The entity whose equity interests are acquired (the legal acquired operation) must be the acquirer for accounting purposes for the transaction to be considered a reverse acquisition. For example, reverse acquisitions sometimes occur when an ~~unlisted public sector~~ entity wants to become a listed entity but does not want to register its equity shares. To accomplish that, the ~~unlisted public sector~~ entity will arrange for a listed entity to acquire its equity interests in exchange for the equity interests of the listed entity. In this example, the listed entity is the legal acquirer because it issued its equity interests, and the ~~unlisted public sector~~ entity is the legal acquired operation because its equity interests were acquired. However, application of the guidance in paragraphs AG10–AG18 results in identifying:

- (a) The listed entity as the acquired operation for accounting purposes (the accounting acquired operation)—i.e., the listed entity does not gain control of one or more operations; and
- (b) The ~~unlisted public sector~~ entity as the acquirer for accounting purposes (the accounting acquirer)—i.e., the ~~unlisted public sector~~ entity does gain control of one or more operations.

The accounting acquired operation must meet the definition of an operation for the transaction to be accounted for as a reverse acquisition, and all of the recognition and measurement principles in this Standard, including the requirement to recognise goodwill, apply.

### Measuring the Consideration Transferred

AG67. In a reverse acquisition, the accounting acquirer usually issues no consideration for the acquired operation. Instead, the accounting acquired operation usually issues its equity shares to the owners of the accounting acquirer. Accordingly, the acquisition-date fair value of the consideration transferred by the accounting acquirer for its interest in the accounting acquired operation is based on the number of equity interests the legal controlled entity would have had to issue to give the owners of the legal controlling entity the same percentage equity interest in the combined entity that results from the reverse acquisition. The fair value of the number of equity interests calculated in that way can be used as the fair value of consideration transferred in exchange for the acquired operation.

### Preparation and Presentation of Consolidated Financial Statements

AG68. Consolidated financial statements prepared following a reverse acquisition are issued under the name of the legal controlling entity (accounting acquired operation) but described in the notes as a continuation of the financial statements of the legal controlled entity (accounting acquirer), with one adjustment, which is to adjust retroactively the accounting acquirer's legal capital to reflect the legal capital of the accounting acquired operation. That adjustment is required to reflect the capital of the legal controlling entity (the accounting acquired operation). Comparative information presented in those consolidated financial statements also is retroactively adjusted to reflect the legal capital of the legal controlling entity (accounting acquired operation).

AG69. Because the consolidated financial statements represent the continuation of the financial statements of the legal controlled entity except for its capital structure, the consolidated financial statements reflect:

- (a) The assets and liabilities of the legal controlled entity (the accounting acquirer) recognised and measured at their pre-combination carrying amounts.

- (b) The assets and liabilities of the legal controlling entity (the accounting acquired operation) recognised and measured in accordance with this Standard.
- (c) The ~~accumulated surplus or deficit~~accumulated comprehensive revenue and expense and other equity balances of the legal controlled entity (accounting acquirer) before the acquisition.
- (d) The amount recognised as issued equity interests in the consolidated financial statements determined by adding the issued equity interest of the legal controlled entity (the accounting acquirer) outstanding immediately before the acquisition to the fair value of the legal controlling entity (accounting acquired operation). However, the equity structure (i.e., the number and type of equity interests issued) reflects the equity structure of the legal controlling entity (the accounting acquired operation), including the equity interests the legal controlling entity issued to effect the acquisition. Accordingly, the equity structure of the legal controlled entity (the accounting acquirer) is restated using the exchange ratio established in the acquisition agreement to reflect the number of shares of the legal controlling entity (the accounting acquired operation) issued in the reverse acquisition.
- (e) The non-controlling interest's proportionate share of the legal controlled entity's (accounting acquirer's) pre-acquisition carrying amounts of retained earnings and other equity interests as discussed in paragraphs AG70 and AG71.

#### Non-Controlling Interest

- AG70. In a reverse acquisition, some of the owners of the legal acquired operation (the accounting acquirer) might not exchange their equity interests for equity interests of the legal controlling entity (the accounting acquired operation). Those owners are treated as a non-controlling interest in the consolidated financial statements after the reverse acquisition. That is because the owners of the legal acquired operation that do not exchange their equity interests for equity interests of the legal acquirer have an interest in only the results and net assets of the legal acquired operation—not in the results and net assets of the combined entity. Conversely, even though the legal acquirer is the acquired operation for accounting purposes, the owners of the legal acquirer have an interest in the results and net assets of the combined entity.
- AG71. The assets and liabilities of the legal acquired operation are measured and recognised in the consolidated financial statements at their pre-combination carrying amounts (see paragraph AG69(a)). Therefore, in a reverse acquisition the non-controlling interest reflects the non-controlling shareholders' proportionate interest in the pre-acquisition carrying amounts of the legal acquired operation's net assets even if the non-controlling interests in other acquisitions are measured at their fair value at the acquisition date.

#### *Recognising Particular Assets Acquired and Liabilities Assumed in an Acquisition (see paragraphs 64–68)*

##### Operating Leases

- AG72. The acquirer shall recognise no assets or liabilities related to an operating lease in which the acquired operation is the lessee except as required by paragraphs AG73–AG74.
- AG73. The acquirer shall determine whether the terms of each operating lease in which the acquired operation is the lessee are favourable or unfavourable. The acquirer shall recognise an intangible asset if the terms of an operating lease are favourable relative to market terms and a liability if the terms are unfavourable relative to market terms. Paragraph AG89 provides guidance on measuring the acquisition-date fair value of assets subject to operating leases in which the acquired operation is the lessor.
- AG74. An identifiable intangible asset may be associated with an operating lease, which may be evidenced by market participants' willingness to pay a price for the lease even if it is at market terms. For example, a lease of gates at an airport or of retail space in a prime shopping area might provide entry into a market or other future economic benefits or service potential that qualify as identifiable intangible assets, for example, as a relationship with users of a service. In that situation, the acquirer shall recognise the associated identifiable intangible asset(s) in accordance with paragraph AG75.



## Intangible Assets

- AG75. The acquirer shall recognise, separately from goodwill, the identifiable intangible assets acquired in an acquisition. An intangible asset is identifiable if it meets either the separability criterion or the binding arrangement criterion.
- AG76. An intangible asset that meets the binding arrangement criterion is identifiable even if the asset is not transferable or separable from the acquired operation or from other rights and obligations. For example:
- (a) An acquired operation leases a facility under an operating lease that has terms that are favourable relative to market terms. The lease terms explicitly prohibit transfer of the lease (through either sale or sublease). The amount by which the lease terms are favourable compared with the terms of current market transactions for the same or similar items is an intangible asset that meets the binding arrangement criterion for recognition separately from goodwill, even though the acquirer cannot sell or otherwise transfer the lease arrangement.
  - (b) An acquired operation owns and operates a nuclear power plant. The licence to operate that power plant is an intangible asset that meets the binding arrangement criterion for recognition separately from goodwill, even if the acquirer cannot sell or transfer it separately from the acquired power plant. An acquirer may recognise the fair value of the operating licence and the fair value of the power plant as a single asset for financial reporting purposes if the useful lives of those assets are similar.
  - (c) An acquired operation owns a technology patent. It has licensed that patent to others for their exclusive use outside the domestic market, receiving a specified percentage of future foreign revenue in exchange. Both the technology patent and the related licence agreement meet the binding arrangement criterion for recognition separately from goodwill even if selling or exchanging the patent and the related licence agreement separately from one another would not be practical.
- AG77. The separability criterion means that an acquired intangible asset is capable of being separated or divided from the acquired operation and sold, transferred, licensed, rented or exchanged, either individually or together with a related binding arrangement, identifiable asset or liability. An intangible asset that the acquirer would be able to sell, license or otherwise exchange for something else of value meets the separability criterion even if the acquirer does not intend to sell, license or otherwise exchange it. An acquired intangible asset meets the separability criterion if there is evidence of exchange transactions for that type of asset or an asset of a similar type, even if those transactions are infrequent and regardless of whether the acquirer is involved in them. For example, lists of users of a service are frequently licensed and thus meet the separability criterion. Even if an acquired operation believes its lists of users of a service have characteristics different from other lists of users of a service, the fact that lists of users of a service are frequently licensed generally means that the acquired list of users of a service meets the separability criterion. However, a list of users of a service acquired in an acquisition would not meet the separability criterion if the terms of confidentiality or other agreements prohibit an entity from selling, leasing or otherwise exchanging information about its users of a service.
- AG78. An intangible asset that is not individually separable from the acquired operation or combined entity meets the separability criterion if it is separable in combination with a related binding arrangement, identifiable asset or liability. For example, an acquired operation owns a registered trademark and documented but unpatented technical expertise used to manufacture the trademarked product. To transfer ownership of a trademark, the owner is also required to transfer everything else necessary for the new owner to produce a product or service indistinguishable from that produced by the former owner. Because the unpatented technical expertise must be separated from the acquired operation or combined entity and sold if the related trademark is sold, it meets the separability criterion.

## Reacquired Rights

- AG79. As part of an acquisition, an acquirer may reacquire a right that it had previously granted to the acquired operation to use one or more of the acquirer's recognised or unrecognised assets. Examples of such rights include a [right to use the acquirer's trade name under a network or partner agreement or a right to use the acquirer's technology under a technology licensing agreement](#). A reacquired right is an identifiable intangible asset that the acquirer recognises separately from goodwill or a gain from a bargain purchase. Paragraph 83 provides guidance on measuring a reacquired right and paragraph 113 provides guidance on the subsequent accounting for a reacquired right.

- AG80. If the terms of the binding arrangement giving rise to a reacquired right are favourable or unfavourable relative to the terms of current market transactions for the same or similar items, the acquirer shall recognise a settlement gain or loss. Paragraph AG100 provides guidance for measuring that settlement gain or loss.

#### Assembled Workforce and Other Items that are not Identifiable

- AG81. The acquirer subsumes into goodwill the value of an acquired intangible asset that is not identifiable as of the acquisition date. For example, an acquirer may attribute value to the existence of an assembled workforce, which is an existing collection of employees that permits the acquirer to continue to operate an acquired operation from the acquisition date. An assembled workforce does not represent the intellectual capital of the skilled workforce—the (often specialised) knowledge and experience that employees of an acquired operation bring to their jobs. Because the assembled workforce is not an identifiable asset to be recognised separately from goodwill or a gain from a bargain purchase, any value attributed to it is subsumed into goodwill or a gain from a bargain purchase.
- AG82. The acquirer also subsumes into goodwill or a gain from a bargain purchase any value attributed to items that do not qualify as assets at the acquisition date. For example, the acquirer might attribute value to potential binding arrangements the acquired operation is negotiating with prospective new customers at the acquisition date. Because those potential binding arrangements are not themselves assets at the acquisition date, the acquirer does not recognise them separately from goodwill or a gain from a bargain purchase. The acquirer should not subsequently reclassify the value of those binding arrangements from goodwill for events that occur after the acquisition date. However, the acquirer should assess the facts and circumstances surrounding events occurring shortly after the acquisition to determine whether a separately recognizable intangible asset existed at the acquisition date.
- AG83. After initial recognition, an acquirer accounts for intangible assets acquired in an acquisition in accordance with the provisions of PBE IPSAS 31. However, as described in paragraph 6 of PBE IPSAS 31, the accounting for some acquired intangible assets after initial recognition is prescribed by other PBE Standards.
- AG84. The identifiability criteria determine whether an intangible asset is recognised separately from goodwill. However, the criteria neither provide guidance for measuring the fair value of an intangible asset nor restrict the assumptions used in measuring the fair value of an intangible asset. For example, the acquirer would take into account the assumptions that market participants would use when pricing the intangible asset, such as expectations of future renewals of binding arrangements, in measuring fair value. It is not necessary for the renewals themselves to meet the identifiability criteria. (However, see paragraph 83, which establishes an exception to the fair value measurement principle for reacquired rights recognised in an acquisition.) Paragraphs 39.4D and 39.5E of PBE IPSAS 31 provide guidance for determining whether intangible assets should be combined into a single unit of account with other intangible or tangible assets.

#### *Forgiveness of Amounts of Tax Due in an Acquisition (where Included in the Terms of the Acquisition) (see paragraphs 78–79.1)*

- AG85. The acquirer shall not recognise any amounts in respect of an acquired operation's tax due where these amounts have been forgiven by a tax authority as part of the terms of the acquisition. Where tax forgiveness occurs subsequent to an acquisition, the resulting entity applies the requirements in paragraph 118. The acquirer shall account for an acquired operation's tax due that has not been forgiven by a tax authority in accordance with PBE IAS 12~~the relevant international or national accounting standard dealing with income taxes.~~
- AG86. ~~[Not used] If the acquirer is itself the tax authority, it shall derecognise any tax receivable relating to the acquired operation's tax due that has been forgiven in accordance with PBE IPSAS 23.~~

Agenda item 7.1 reference: Tax forgiven (paras 22–27)
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- AG87. If, as a consequence of the terms of an acquisition, a tax authority forgives an amount of the acquirer's tax due, the acquirer shall derecognise those amounts in accordance with PBE IAS 12~~the relevant international or national accounting standard dealing with income taxes.~~



*Measuring the Fair Value of Particular Identifiable Assets and a Non-Controlling Interest in an Acquired Operation in an Acquisition (see paragraphs 72–73)*

Assets with Uncertain Cash Flows (Valuation Allowances)

- AG88. The acquirer shall not recognise a separate valuation allowance as of the acquisition date for assets acquired in an acquisition that are measured at their acquisition-date fair values because the effects of uncertainty about future cash flows are included in the fair value measure. For example, because this Standard requires the acquirer to measure acquired receivables, including loans, at their acquisition-date fair values in accounting for an acquisition, the acquirer does not recognise a separate valuation allowance for the cash flows of the binding arrangement that are deemed to be uncollectible at that date<sup>11</sup>.

Assets Subject to Operating Leases in which the Acquired Operation is the Lessor

- AG89. In measuring the acquisition-date fair value of an asset such as a building that is subject to an operating lease in which the acquired operation is the lessor, the acquirer shall take into account the terms of the lease. In other words, the acquirer does not recognise a separate asset or liability if the terms of an operating lease are either favourable or unfavourable when compared with market terms as paragraph AG73 requires for leases in which the acquired operation is the lessee.

Assets that the Acquirer Intends not to use or to use in a Way that is Different from the Way Other Market Participants would use them

- AG90. To protect its competitive position, or for security or other reasons, the acquirer may intend not to use an acquired non-financial asset actively, or it may not intend to use the asset according to its highest and best use. For example, that might be the case for an acquired research and development intangible asset that the acquirer plans to use defensively by preventing others from using it. Nevertheless, the acquirer shall measure the fair value of the non-financial asset assuming its highest and best use by market participants in accordance with the appropriate valuation premise, both initially and when measuring fair value less costs of disposal for subsequent impairment testing.

Non-Controlling Interest in an Acquired Operation

- AG91. This Standard allows the acquirer to measure a non-controlling interest in the acquired operation at its fair value at the acquisition date. Sometimes an acquirer will be able to measure the acquisition-date fair value of a non-controlling interest on the basis of a quoted price in an active market for the equity shares (i.e., those not held by the acquirer). In other situations, however, a quoted price in an active market for the equity shares will not be available. In those situations, the acquirer would measure the fair value of the non-controlling interest using other valuation techniques.
- AG92. The fair values of the acquirer's interest in the acquired operation and the non-controlling interest on a per-share basis might differ. The main difference is likely to be the inclusion of a control premium in the per-share fair value of the acquirer's interest in the acquired operation or, conversely, the inclusion of a discount for lack of control (also referred to as a non-controlling interest discount) in the per-share fair value of the non-controlling interest if market participants would take into account such a premium or discount when pricing the non-controlling interest.

*Measuring Goodwill or a Gain from a Bargain Purchase in an Acquisition (see paragraphs 85–98)*

Relationship between Goodwill and Cash Flows (see paragraph 86)

- AG93. The acquirer shall recognise goodwill only to the extent that the acquirer estimates there will be favourable changes to its net cash flows, either from increased cash inflows or decreased cash outflows. An acquirer shall not recognise goodwill related to service potential other than cash flows.

<sup>11</sup> If an entity that applies this Standard and early adopts PBE IFRS 9, this paragraph should be read as follows:

The acquirer shall not recognise a separate valuation allowance as of the acquisition date for assets acquired in an acquisition that are measured at their acquisition-date fair values because the effects of uncertainty about future cash flows are included in the fair value measure. For example, because this Standard requires the acquirer to measure acquired receivables, including loans, at their acquisition-date fair values in accounting for an acquisition, the acquirer does not recognise a separate valuation allowance for the cash flows of the binding arrangement that are deemed to be uncollectible at that date, or a loss allowance for expected credit losses.

Measuring the Acquisition-Date Fair Value of the Acquirer's Interest in the Acquired Operation Using Valuation Techniques (see paragraph 87)

- AG94. In an acquisition achieved without the transfer of consideration, the acquirer must substitute the acquisition-date fair value of its interest in the acquired operation for the acquisition-date fair value of the consideration transferred to measure goodwill, a loss or a gain on a bargain purchase (see paragraphs 85–87).

Special Considerations in Applying the Acquisition Method to Combinations of Mutual Entities (Application of paragraph 87)

- AG95. When two mutual entities combine, the fair value of the equity or member interests in the acquired operation (or the fair value of the acquired operation) may be more reliably measurable than the fair value of the member interests transferred by the acquirer. In that situation, paragraph 87 requires the acquirer to determine the amount of goodwill by using the acquisition-date fair value of the acquired operation's equity interests instead of the acquisition-date fair value of the acquirer's equity interests transferred as consideration. In addition, the acquirer in a combination of mutual entities shall recognise the acquired operation's net assets as a direct addition to capital or equity in its statement of financial position, not as an addition to ~~accumulated surplus or deficit~~accumulated comprehensive revenue and expense, which is consistent with the way in which other types of entities apply the acquisition method.
- AG96. Although they are similar in many ways to other entities, mutual entities have distinct characteristics that arise primarily because their members are both customers and owners. Members of mutual entities generally expect to receive benefits for their membership, often in the form of reduced fees charged for goods and services or patronage dividends. The portion of patronage dividends allocated to each member is often based on the amount of business the member did with the mutual entity during the year.
- AG97. A fair value measurement of a mutual entity should include the assumptions that market participants would make about future member benefits as well as any other relevant assumptions market participants would make about the mutual entity. For example, a present value technique may be used to measure the fair value of a mutual entity. The cash flows used as inputs to the model should be based on the expected cash flows of the mutual entity, which are likely to reflect reductions for member benefits, such as reduced fees charged for goods and services.

*Determining what is Part of the Acquisition Transaction (see paragraphs 109–111)*

- AG98. The acquirer should consider the following factors, which are neither mutually exclusive nor individually conclusive, to determine whether a transaction is part of the exchange for the acquired operation or whether the transaction is separate from the acquisition:
- (a) The reasons for the transaction. Understanding the reasons why the parties to the acquisition (the acquirer and the acquired operation and their owners, directors and managers—and their agents) entered into a particular transaction or arrangement may provide insight into whether it is part of the consideration transferred and the assets acquired or liabilities assumed. For example, if a transaction is arranged primarily for the benefit of the acquirer or the combined entity rather than primarily for the benefit of the acquired operation or its former owners before the combination, that portion of the transaction price paid (and any related assets or liabilities) is less likely to be part of the exchange for the acquired operation. Accordingly, the acquirer would account for that portion separately from the acquisition.
  - (b) Who initiated the transaction. Understanding who initiated the transaction may also provide insight into whether it is part of the exchange for the acquired operation. For example, a transaction or other event that is initiated by the acquirer may be entered into for the purpose of providing future economic benefits to the acquirer or combined entity with little or no benefit received by the acquired operation or its former owners before the combination. On the other hand, a transaction or arrangement initiated by the acquired operation or its former owners is less likely to be for the benefit of the acquirer or the combined entity and more likely to be part of the acquisition transaction.
  - (c) The timing of the transaction. The timing of the transaction may also provide insight into whether it is part of the exchange for the acquired operation. For example, a transaction between the acquirer and the acquired operation that takes place during the negotiations of the terms of

an acquisition may have been entered into in contemplation of the acquisition to provide future economic benefits to the acquirer or the combined entity. If so, the acquired operation or its former owners before the acquisition are likely to receive little or no benefit from the transaction except for benefits they receive as part of the combined entity.

Effective Settlement of a Pre-Existing Relationship between the Acquirer and Acquired Operation in an Acquisition (see paragraph 110(a))

- AG99. The acquirer and acquired operation may have a relationship that existed before they contemplated the acquisition, referred to here as a ‘pre-existing relationship’. A pre-existing relationship between the acquirer and acquired operation may arise from a binding arrangement (for example, vendor and customer or licensor and licensee) or may arise outside of a binding arrangement (for example, plaintiff and defendant).
- AG100. If the acquisition in effect settles a pre-existing relationship, the acquirer recognises a gain or loss, measured as follows:
- (a) For a pre-existing relationship arising outside of a binding arrangement (such as a lawsuit), fair value.
  - (b) For a pre-existing relationship arising from a binding arrangement, the lesser of (i) and (ii):
    - (i) The amount by which the binding arrangement is favourable or unfavourable from the perspective of the acquirer when compared with terms for current market transactions for the same or similar items. (An unfavourable binding arrangement is a binding arrangement that is unfavourable in terms of current market terms. It is not necessarily an onerous binding arrangement in which the unavoidable costs of meeting the obligations under the binding arrangement exceed the economic benefits expected to be received under it.)
    - (ii) The amount of any stated settlement provisions in the binding arrangement available to the counterparty to whom the binding arrangement is unfavourable.

If (ii) is less than (i), the difference is included as part of the acquisition accounting.

The amount of gain or loss recognised may depend in part on whether the acquirer had previously recognised a related asset or liability, and the reported gain or loss therefore may differ from the amount calculated by applying the above requirements.

- AG101. A pre-existing relationship may be a binding arrangement that the acquirer recognises as a reacquired right. If the binding arrangement includes terms that are favourable or unfavourable when compared with pricing for current market transactions for the same or similar items, the acquirer recognises, separately from the acquisition, a gain or loss for the effective settlement of the binding arrangement, measured in accordance with paragraph AG100.

Arrangements for Contingent Payments to Employees or Selling Shareholders (see paragraph 110(b))

- AG102. Whether arrangements for contingent payments to employees or selling shareholders are contingent consideration in the acquisition or are separate transactions depends on the nature of the arrangements. Understanding the reasons why the acquisition agreement includes a provision for contingent payments, who initiated the arrangement and when the parties entered into the arrangement may be helpful in assessing the nature of the arrangement.
- AG103. If it is not clear whether an arrangement for payments to employees or selling shareholders is part of the exchange for the acquired operation or is a transaction separate from the acquisition, the acquirer should consider the following indicators:
- (a) Continuing employment. The terms of continuing employment by the selling shareholders who become key employees may be an indicator of the substance of a contingent consideration arrangement. The relevant terms of continuing employment may be included in an employment agreement, acquisition agreement or some other document. A contingent consideration arrangement in which the payments are automatically forfeited if employment terminates is remuneration for post-combination services. Arrangements in which the contingent payments are not affected by employment termination may indicate that the contingent payments are additional consideration rather than remuneration.

- (b) Duration of continuing employment. If the period of required employment coincides with or is longer than the contingent payment period, that fact may indicate that the contingent payments are, in substance, remuneration.
- (c) Level of remuneration. Situations in which employee remuneration other than the contingent payments is at a reasonable level in comparison with that of other key employees in the combined entity may indicate that the contingent payments are additional consideration rather than remuneration.
- (d) Incremental payments to employees. If selling shareholders who do not become employees receive lower contingent payments on a per-share basis than the selling shareholders who become employees of the combined entity, that fact may indicate that the incremental amount of contingent payments to the selling shareholders who become employees is remuneration.
- (e) Number of shares owned. The relative number of shares owned by the selling shareholders who remain as key employees may be an indicator of the substance of the contingent consideration arrangement. For example, if the selling shareholders who owned substantially all of the shares in the acquired operation continue as key employees, that fact may indicate that the arrangement is, in substance, a profit-sharing arrangement intended to provide remuneration for post-combination services. Alternatively, if selling shareholders who continue as key employees owned only a small number of shares of the acquired operation and all selling shareholders receive the same amount of contingent consideration on a per-share basis, that fact may indicate that the contingent payments are additional consideration. The pre-acquisition ownership interests held by parties related to selling shareholders who continue as key employees, such as family members, should also be considered.
- (f) Linkage to the valuation. If the initial consideration transferred at the acquisition date is based on the low end of a range established in the valuation of the acquired operation and the contingent formula relates to that valuation approach, that fact may suggest that the contingent payments are additional consideration. Alternatively, if the contingent payment formula is consistent with prior profit-sharing arrangements, that fact may suggest that the substance of the arrangement is to provide remuneration.
- (g) Formula for determining consideration. The formula used to determine the contingent payment may be helpful in assessing the substance of the arrangement. For example, if a contingent payment is determined on the basis of a multiple of earnings, that might suggest that the obligation is contingent consideration in the acquisition and that the formula is intended to establish or verify the fair value of the acquired operation. In contrast, a contingent payment that is a specified percentage of earnings might suggest that the obligation to employees is a profit-sharing arrangement to remunerate employees for services rendered.
- (h) Other agreements and issues. The terms of other arrangements with selling shareholders (such as agreements not to compete, executory contracts, consulting contracts and property lease agreements) and the income tax treatment of contingent payments may indicate that contingent payments are attributable to something other than consideration for the acquired operation. For example, in connection with the acquisition, the acquirer might enter into a property lease arrangement with a significant selling shareholder. If the lease payments specified in the lease arrangement are significantly below market, some or all of the contingent payments to the lessor (the selling shareholder) required by a separate arrangement for contingent payments might be, in substance, payments for the use of the leased property that the acquirer should recognise separately in its post-combination financial statements. In contrast, if the lease arrangement specifies lease payments that are consistent with market terms for the leased property, the arrangement for contingent payments to the selling shareholder may be contingent consideration in the acquisition.

Acquirer Share-Based Payment Awards Exchanged for Awards held by the Acquired Operation's Employees (see paragraph 110(b))

- AG104. An acquirer may exchange its share-based payment awards for awards held by employees of the acquired operation. The acquirer shall account for exchanges of share options or other share-based payment awards in conjunction with an acquisition in accordance with the relevant international or national accounting standard dealing with share-based payments.

- AG105. In situations in which acquired operation awards would expire as a consequence of an acquisition and if the acquirer replaces those awards when it is not obliged to do so, the acquirer shall recognise any costs as remuneration cost in the post-combination financial statements in accordance with the relevant international or national accounting standard dealing with share-based payments. The cost of those awards shall not be included in measuring the consideration transferred in the acquisition.

#### Equity-Settled Share-Based Payment Transactions of the Acquired Operation

- AG106. The acquired operation may have outstanding share-based payment transactions that the acquirer does not exchange for its share-based payment transactions. If vested, those acquired operation share-based payment transactions are part of the non-controlling interest in the acquired operation. If unvested, they are measured as if the acquisition date were the grant date. Share-based payment transactions are measured in accordance with the relevant international or national accounting standard dealing with share-based payments.

#### *Subsequent Measurement and Accounting (see paragraph 112)*

- AG107. Examples of other PBE Standards that provide guidance on subsequently measuring and accounting for assets acquired and liabilities assumed or incurred in an acquisition include:
- (a) PBE IPSAS 31 prescribes the accounting for identifiable intangible assets acquired in an acquisition. The acquirer measures goodwill at the amount recognised at the acquisition date less any accumulated impairment losses. PBE IPSAS 26 prescribes the accounting for impairment losses.
  - (b) PBE IPSAS 35 provides guidance on accounting for changes in a controlling entity's ownership interest in a controlled entity after control is obtained.
  - (c) PBE IFRS 4 provides guidance on the subsequent accounting for an insurance contract acquired in an acquisition.
  - (d) PBE IAS 12 prescribes the subsequent accounting for deferred tax assets (including unrecognised deferred tax assets) and liabilities acquired in an acquisition.
- AG108. An acquirer should refer to the relevant international or national accounting standards for guidance on subsequently measuring and accounting for ~~insurance contracts, income taxes and~~ share-based payments.

#### *Subsequent Measurement of Transfers, Concessionary Loans and Similar Benefits Received by an Acquirer or Acquired Operation on the Basis of Criteria that may Change as a Result of an Acquisition (see paragraph 114)*

- AG109. Prior to an acquisition taking place, an acquirer or an acquired operation may receive a transfer from a third party, based on specified criteria. For example, a national government may provide grants to those municipalities where the municipality's revenue per head of population is below a threshold. An acquisition by a municipality of a cash-generating operation may increase the revenue per head of population of the municipality so that it is above the threshold. This may cause the government to review the grant.
- AG110. The acquirer shall not account for any revisions to the grant amount as part of the acquisition, but accounts for any revisions at the point the grantor makes its intentions known in accordance with other PBE Standards.
- AG111. Similar circumstances may arise in respect of concessionary loans and other benefits. The acquirer shall not account for any revisions to those transactions as part of the acquisition, but accounts for any revisions at the point the grantor makes its intentions known in accordance with other PBE Standards.

#### *Acquisitions Occurring During a Reporting Period*

- AG112. The resulting entity meets the needs of the users of its financial statements for information about the acquired operations prior to the acquisition by making the disclosures in paragraph 120(r).
- AG113. To satisfy the requirements of a regulator, it may be necessary for the acquirer to present or disclose information in addition to that required by this Standard.

**Transitional Provisions for ~~PBE public sector~~ Combinations Involving only Mutual Entities or by Contract Alone (see paragraph 133)**

- AG114. Paragraph -126.1 provides that this Standard applies prospectively to ~~PBE public sector~~ combinations for which the acquisition date or amalgamation date is on or after the beginning of the first annual reporting period beginning on or after [date]. Earlier application is permitted.
- AG115. The requirement to apply this Standard prospectively has the following effect for a ~~PBE public sector~~ combination involving only mutual entities or by contract alone if the acquisition date or amalgamation date for that ~~PBE public sector~~ combination is before the application of this Standard:
- (a) Classification. An entity shall continue to classify the prior ~~PBE public sector~~ combination in accordance with the entity's previous accounting policies for such combinations.
  - (b) Previously recognised goodwill. At the beginning of the first annual period in which this Standard is applied, the carrying amount of goodwill arising from the prior ~~PBE public sector~~ combination shall be its carrying amount at that date in accordance with the entity's previous accounting policies. In determining that amount, the entity shall eliminate the carrying amount of any accumulated amortisation of that goodwill and the corresponding decrease in goodwill. No other adjustments shall be made to the carrying amount of goodwill.
  - (c) Goodwill previously recognised as a deduction from equity. The entity's previous accounting policies may have resulted in goodwill arising from the prior ~~PBE public sector~~ combination being recognised as a deduction from equity. In that situation the entity shall not recognise that goodwill as an asset at the beginning of the first annual period in which this Standard is applied. Furthermore, the entity shall not recognise in surplus or deficit any part of that goodwill when it disposes of all or part of the operation to which that goodwill relates or when a cash-generating unit to which the goodwill relates becomes impaired.
  - (d) Subsequent accounting for goodwill. From the beginning of the first annual period in which this Standard is applied, an entity shall discontinue amortising goodwill arising from the prior ~~PBE public sector~~ combination and shall test goodwill for impairment in accordance with PBE IPSAS 26.
  - (e) Previously recognised negative goodwill. An entity that accounted for the prior ~~PBE public sector~~ combination by applying the purchase method may have recognised a deferred credit for an excess of its interest in the net fair value of the acquired operation's identifiable assets and liabilities over the cost of that interest (sometimes called negative goodwill). If so, the entity shall derecognise the carrying amount of that deferred credit at the beginning of the first annual period in which this Standard is applied with a corresponding adjustment to the opening balance of accumulated ~~comprehensive revenue and expense surplus or deficit~~ at that date.

**Amendments to Other Standards**

[Not included for this Board meeting]

## Basis for Conclusions

*This Basis for Conclusions accompanies, but is not part of, PBE IPSAS 40.*

### Introduction

- BC1. The New Zealand Accounting Standards Board (NZASB) has modified IPSAS 40 *Public Sector Combinations* for application by Tier 1 and Tier 2 public benefit entities (PBEs). Where applicable, disclosure concessions have been identified for Tier 2 entities and the language generalised for use by PBEs. The NZASB considers that the requirements of IPSAS 40 are generally appropriate for application by PBEs.
- BC2. In the interests of coherence within PBE Standards, the NZASB has modified IPSAS 40 to incorporate guidance that relates to other PBE Standards, for which there is no equivalent IPSAS.

### Indicator Relating to Consideration

- BC3. The NZASB removed the indicator in paragraph 12(c) of IPSAS 40. This indicator read:
- Consideration is not paid because there is no-one (whether an individual or an entity) with an entitlement to the net assets of a transferred entity (paragraph AG31 provides additional guidance).*
- BC4. The NZASB removed this indicator because the NZASB was of the view that the absence of consideration does not in itself provide evidence the PBE combination is an amalgamation. The NZASB noted that a donated operation could be an acquisition.
- BC5. The removal of this indicator is also consistent with broader view of the definition of equity interests and owners in New Zealand. In the New Zealand public sector and not-for-profit (NFP) sector, the concept of equity interests is not limited to equity participants in an equity instrument and use of the term owners is not limited to owners with a quantifiable ownership interest.
- BC6. The removal of this indicator led to a number of other changes throughout the Standard. The main changes were:
- (a) adding guidance in paragraph 12(b) to consider reasons why no consideration is paid;
  - (b) the removal of paragraph AG31 which contained guidance on paragraph 12(c);
  - (c) the removal of a reference to this indicator in the illustrative examples (scenario 2 variation, scenario 3 and scenario 14); and
  - (d) the reclassification of illustrative example 6 from an amalgamation to an acquisition.

Agenda item 7.1 reference: Indicator in paragraph 12(c) (paras 10–17)
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## IPSASB Basis for Conclusions

*This Basis for Conclusions accompanies, but is not part of, IPSAS 40*

### Objective (paragraph 1)

- BC1. In the absence of an International Public Sector Accounting Standard (IPSAS) dealing with public sector combinations, public sector entities are directed, in IPSAS 1, *Presentation of Financial Statements*, to look to other international or national accounting standards. In the case of public sector combinations, they may look to International Financial Reporting Standard (IFRS®) 3, *Business Combinations*. However, IFRS 3 requires all business combinations to be accounted for using acquisition accounting. In developing IFRS 3, the International Accounting Standards Board (IASB®) came to the conclusion that ‘true mergers’ or ‘mergers of equals’ in which none of the combining entities obtains control of the others are so rare as to be virtually non-existent. The IASB also observed that respondents and other constituents were unable to suggest an unambiguous and non-arbitrary boundary for distinguishing true mergers or mergers of equals from other business combinations and concluded that developing such an operational boundary would not be feasible (see IFRS 3, BC35). Consequently, the IASB decided that separate accounting requirements for such combinations was not necessary.
- BC2. Many consider that in the public sector, mergers or amalgamations are the most common form of combination. As a result, public sector entities may not apply IFRS Standards when accounting for public sector combinations. This means that there may not be consistent or appropriate reporting of such combinations in general purpose financial statements (GPFSs). Consequently, users may not be able to obtain the information needed to identify the type of public sector combination and evaluate its nature and financial effect. The IPSASB believes this Standard will promote consistency and comparability in how public sector combinations are reported by public sector entities.

### Process

- BC3. In developing this Standard the IPSASB had regard to the discussion of control in IPSAS 35, *Consolidated Financial Statements*. The IPSASB considered how control, as defined in IPSAS 35, should influence the classification of public sector combinations in this Standard. The IPSASB also had regard to the guidance on combinations in the *Government Finance Statistics Manual 2014* (GFSM 2014) with the aim of avoiding unnecessary differences. The IPSASB also considered IFRS 3 and guidance on combinations developed by national standard setters.

### *Alignment with Government Finance Statistics (GFS)*

- BC4. In developing this Standard, the IPSASB had regard to the treatment of public sector combinations in Government Finance Statistics (GFS):

GFS guidelines make a distinction between an acquisition and an amalgamation based on the principle that with an acquisition a transaction occurs, while with an amalgamation just a reclassification of units may occur.

A transaction will occur where a “market unit” is nationalized or privatized (that is, entering government control or leaving it), and the amounts are recorded in GFS as transactions in equity that correspond to the observed transaction price. Any changes in valuation—for example, between the opening balance of a government equity stake and the eventual transaction price—are recorded as revaluation effects, with no impact on government net lending/net borrowing. For amalgamations, the main impact is on the sectorization of the “institutional units”.

Where the units before amalgamation belonged to the same sector or subsector of general government, the amalgamation will have no impact on the data for that sector or subsector. For example, an amalgamation of two local governments, where both are already classified to the local government sector, would not change results for the local government sector.

However, in cases where a unit in one subsector is being amalgamated with a unit in another subsector, the amalgamated units will be removed from the sector they belonged to and be added to the sector of the new amalgamated unit, through a reclassification of the unit (recorded in GFS as an “other volume change in assets and liabilities”). For example, if a local government unit is amalgamated with a state

government, the unit will be reclassified from the local government subsector to the state government subsector.

BC5. The IPSASB agreed the approach in GFS was not an appropriate basis for classifying public sector combinations in this Standard, for the following reasons:

- (a) The approach in GFS is based on a number of concepts that have no equivalent in IPSASs, for example:
  - (i) The classification of institutional units into sectors based on their economic nature; and
  - (ii) The distinction between market producers and nonmarket producers.
- (b) Amalgamations in GFS can arise from a reclassification of units without a transaction being recorded, which is inconsistent with the approach in IPSASs; and
- (c) Public sector combinations within the same sector or subsector of general government have no impact on the data in GFS, whereas IPSASs would require the changes to individual entities to be accounted for.

BC6. In coming to this conclusion the IPSASB noted that the different approaches in GFS and IPSASs may lead to similar accounting, for example:

- (a) Nationalizations are likely to be recorded as acquisitions under both approaches; and
- (b) The modified pooling of interests method of accounting will produce similar accounting to the GFS reclassification approach where the combining operations had previously adopted the same accounting policies.

#### Scope (paragraphs 2–4)

BC7. The IPSASB initially considered developing two Standards on public sector combinations, covering:

- (a) Entity combinations arising from exchange transactions—a limited convergence project with IFRS 3; and
- (b) Entity combinations arising from non-exchange transactions—a public sector-specific project.

BC8. In May 2009, the IPSASB issued Exposure Draft (ED) 41, *Entity Combinations from Exchange Transactions*, which was the limited convergence project with IFRS 3. Following the consultation process on ED 41, the IPSASB decided not to continue with this approach for the following reasons:

- (a) IFRS 3 includes bargain purchases within its scope. It could be argued, therefore, that IFRS 3 also applies to at least some non-exchange entity combinations. The IPSASB acknowledged that it may be difficult to establish a clear demarcation between all exchange and non-exchange entity combinations.
- (b) It was not clear whether combinations where no party gains control of the other parties to the combination would be classified as entity combinations arising from exchange transactions, and therefore required to be accounted for as an acquisition in accordance with ED 41.

BC9. Subsequently, the IPSASB decided to develop a single standard dealing with all public sector combinations. This wider scope was included in the Consultation Paper (CP), *Public Sector Combinations*, issued in June 2012. Respondents to the CP supported this wider scope.

BC10. The IPSASB, therefore, decided that this Standard should apply to all public sector combinations, with only limited exceptions. This Standard defines a public sector combination as the bringing together of separate operations into one public sector entity. This definition refers to the bringing together of operations rather than entities, as public sector combinations, in common with business combinations, may involve part of an entity that can be managed separately from the rest of the entity.

BC11. In coming to a decision on the scope of this Standard, the IPSASB agreed to include public sector combinations under common control. While these are excluded from the scope of IFRS 3, the IPSASB considered it important that this Standard included all public sector combinations within its scope.

*Scope exclusions*

- BC12. The IPSASB agreed that this Standard should not apply to the formation of joint arrangements or joint ventures. The IPSASB stated in the CP that:
- “The concept underlying the formation of a joint venture differs from other combinations, in that the formation arises from separate entities deciding to share control, i.e., they have joint control of the operations that form the joint venture. The concept of joint control may give rise to issues that affect how the joint venture itself should account for its formation.”
- BC13. In developing this Standard, the IPSASB discussed whether this rationale was still valid given that this Standard takes a different approach to classifying public sector combinations. The IPSASB concluded that the concept of joint control does not reflect the issues addressed in this Standard, and agreed to exclude the formation of joint arrangements or joint ventures from its scope.
- BC14. The IPSASB noted that combinations of two or more joint arrangements may occur. The IPSASB considered that, where such a combination results in the formation of a new joint arrangement, this would be outside the scope of IPSAS 40. The IPSASB noted that a combination may result in the acquisition of one or more joint arrangements by another joint arrangement. In such circumstances, the entities that previously had control over the acquired joint arrangements give up that joint control. Such a combination would be an acquisition within the scope of IPSAS 40.
- BC15. The IPSASB also agreed to exclude from the scope of this Standard the acquisition by an investment entity of an investment in a controlled entity that is required to be measured at fair value through surplus or deficit. Such transactions are considered to be investments rather than public sector combinations. IPSAS 35 prescribes the accounting requirements for such transactions.

*Responses to ED 60, Public Sector Combinations*

- BC16. The IPSASB issued its proposals in ED 60, *Public Sector Combinations*, in January 2016. Respondents to ED 60 generally supported the proposed scope and the exclusions. The IPSASB considered the responses, and agreed that no changes to the scope were required. In doing so, the IPSASB noted that the scope of the standard included combinations undertaken on a temporary basis, for example the bailout of a private sector company with the intention of selling that company as soon as it was returned to a sound financial position. The IPSASB noted that including such combinations within the scope of this Standard was consistent with the decision taken in developing IPSAS 35 not to require a different accounting treatment for temporarily controlled entities.

**Classification of Public Sector Combinations (paragraphs 7–14)**

- BC17. As a result of the responses it received to ED 41, the IPSASB concluded that distinguishing between entity combinations arising from exchange transactions and entity combinations arising from non-exchange transactions did not provide a suitable basis for a future IPSAS. Relying on the definition of “exchange transactions” in the IPSASB’s literature would mean that most government interventions during times of economic crisis, such as the global financial crisis in 2008, would not meet the definition of an acquisition. The IPSASB considered it inappropriate to define such “bailouts” as amalgamations.
- BC18. The IPSASB also noted that IFRS 3 applied to a “business”, not to an entity. As well as applying to an entity, the definition of a business could also apply to part of an entity that could be managed separately from the rest of the entity. The IPSASB had regard to these issues in developing its approach in the CP.

*Classification approach in the Consultation Paper, Public Sector Combinations*

- BC19. The approach taken in the CP was to distinguish between combinations where the parties to the combination are under common control, and combinations where the parties to the combination are not controlled by the same ultimate controlling party, i.e., not under common control. A further distinction was made between combinations where one party gains control of another party (considered by the CP to be acquisitions), and combinations where no party gains control of the other parties to the combination (considered by the CP to be amalgamations).
- BC20. The IPSASB considered that the concept of control was important in determining the classification of a public sector combination. Control underpins much of financial reporting. IPSAS 35 requires an entity to consolidate those other entities that it controls, as does the predecessor standard, IPSAS 6,

*Consolidated and Separate Financial Statements.* The IPSASB also noted that Government Finance Statistics adopts a similar approach to control as that adopted in both IPSAS 35 and IPSAS 6.

BC21. Similarly, control is an important factor when recognizing assets. Paragraph 5.6 of the *Conceptual Framework for General Purpose Financial Reporting by Public Sector Entities* (the Conceptual Framework) defines an asset as “A resource presently controlled by the entity as a result of a past event.”

BC22. The IPSASB determined, therefore, that control was an appropriate starting point for the classification of public sector combinations. As a result, the CP included the IPSASB’s preliminary view as to the role of control in classifying public sector combinations:

“The sole definitive criterion for distinguishing an amalgamation from an acquisition is that, in an amalgamation, none of the combining operations gains control of the other operations.”

BC23. In developing the CP, the IPSASB explained that the parties to a public sector combination under common control are ultimately controlled by the same entity both before and after the combination. This leads to economic differences between combinations that take place under common control and those that take place not under common control, as follows:

- (a) Public sector combinations between entities within an economic entity (i.e., under common control) do not change the economic resources of that economic entity;
- (b) Any surpluses and deficits resulting from a public sector combination under common control are eliminated in full in the ultimate controlling entity’s consolidated GPFs; and
- (c) The ultimate controlling entity can specify whether any consideration is transferred (and if consideration is transferred, the amount of that consideration) in a public sector combination under common control.

These differences may have implications for the accounting treatment of a public sector combination under common control.

BC24. The approach in the CP reflected the IPSASB’s views that:

- (a) The economic differences between combinations that take place under common control and those that take place not under common control may have implications for their accounting treatment; and
- (b) Acquisitions should be distinguished from amalgamations on the basis of control.

BC25. Similar numbers of respondents to the CP supported and disagreed with the proposals. Respondents who disagreed with the proposals suggested that distinguishing acquisitions from amalgamations based solely on control did not reflect public sector circumstances. In particular, these respondents noted that

- (a) Public sector combinations may occur where it is not possible to identify an acquirer even if it is possible to identify an entity that has gained control of operations as a result of the public sector combination. Under IFRS 3, the acquirer can be identified by analyzing the ownership interests in the respective parties. However, in the public sector there may be no quantifiable ownership interests in the entities, making such an analysis impossible. The entity gaining control of the operations may not have existed prior to the combination, and if there are no quantifiable ownership interests in that entity, it will not be possible to identify an acquirer.
- (b) Public sector combinations may be imposed on all parties to the combination by a higher level of government, for example when a central government reorganizes local government by legislating the combination of municipalities irrespective of the wishes of those municipalities.

BC26. Respondents who disagreed with the proposals in the CP suggested a number of alternative bases for classifying public sector combinations, including:

- (a) Variations of whether consideration was transferred:
  - (i) Consideration was transferred as part of the combination;
  - (ii) Significant consideration was transferred as part of the combination;
  - (iii) The combination was effected at market value;

- (iv) Distinguishing acquisitions (which include the transfer of consideration) not under common control from all other combinations; and
  - (v) Distinguishing between combinations under common control on the basis of whether the combination has “commercial substance” (which includes the transfer of consideration).
- (b) Whether the public sector combination was effected voluntarily or involuntarily.

*Development of the classification approach in ED 60, Public Sector Combinations*

- BC27. The IPSASB considered the responses to the CP. The IPSASB accepted that the classification approach adopted in the CP would not always reflect public sector circumstances. Consequently, the IPSASB agreed to revisit the classification of public sector combinations.
- BC28. As part of this process, the IPSASB considered whether any of the approaches suggested by respondents might provide an alternative basis for classification. The IPSASB concluded that these approaches were not suitable, for the following reasons:
- (a) The IPSASB came to the view that the transfer of consideration, on its own, was insufficient to distinguish an acquisition from an amalgamation. As noted in paragraph BC17 above, defining an acquisition as an exchange transaction would lead to bailouts being classified as amalgamations. Similarly, if an acquisition was defined as requiring consideration to be transferred by the acquirer, this could lead to bailouts being classified as amalgamations. Definitions of an acquisition that required the transfer of significant consideration, or for the public sector combination to take place at market value, would not address issues such as bargain purchases (discussed above in paragraph BC8(a)).
  - (b) The IPSASB came to the view that whether a public sector combination was effected voluntarily or involuntarily did not provide, on its own, sufficient information to classify a public sector combination. The voluntary or involuntary nature of a public sector combination provides information as to the process of the combination but not its outcome. Public sector combinations may have different economic outcomes irrespective of their voluntary or involuntary nature. The IPSASB did not consider that it was possible to classify a public sector combination without considering the outcome of that combination. Consequently, the IPSASB did not consider a classification based solely on the voluntary or involuntary nature of the public sector combination would meet the objectives of financial reporting.
- BC29. The IPSASB reviewed the role of control in classifying public sector combinations, and concluded that control remained an important factor in determining whether a combination was an acquisition or an amalgamation. In coming to this conclusion, the IPSASB noted that an acquisition could only occur when a party to the combination gained control of one or more operations (this is discussed in more detail in paragraph BC25(a) above). Consequently, the IPSASB reviewed the factors suggested by respondents to the CP to determine which factors might usefully supplement the concept of control.
- BC30. The IPSASB discussed the following factors, and agreed that they could be helpful in supplementing the concept of control in classifying public sector combinations:
- (a) **Consideration.** The IPSASB agreed that whether a public sector combination includes the transfer of consideration is relevant to classifying the combination. Acquisitions generally include consideration, whereas consideration will be absent from amalgamations. For the reasons given in paragraph BC28(a) above, the IPSASB agreed that the transfer of consideration in itself was not conclusive, and that more information about the nature of a combination would be obtained by having regard to the reasons why consideration was or was not transferred.
  - (b) **Exchange transactions.** The IPSASB agreed that an acquisition was more likely to occur in an exchange transaction than in a non-exchange transaction. However, the IPSASB had already acknowledged that it may be difficult to establish a clear demarcation between all exchange and non-exchange entity combinations (see paragraph BC8(a) above). The IPSASB came to the conclusion that information about whether a public sector combination was an exchange transaction or a non-exchange transaction could be determined by having regard to the reasons why consideration was or was not transferred. Consequently, the IPSASB concluded that it is not necessary to assess this factor independently of consideration.
  - (c) **Quantifiable ownership interests.** The IPSASB noted that whether there are quantifiable ownership interests in an operation can influence the economic substance of a public sector

combination. If there are no quantifiable ownership interests in an operation, no consideration can be transferred as there is no party with an entitlement to receive the consideration. This can distinguish the combination from an acquisition, where there is always an owner to receive the consideration. The IPSASB noted that that lack of quantifiable ownership interests could be a reason why consideration was not transferred. Consequently, the IPSASB concluded that it is not necessary to assess this factor independently of consideration.

- (d) **Decision-making process.** The IPSASB agreed that having regard to which parties were able to make decisions regarding a public sector combination could provide useful information about the classification of that combination. In the private sector, combinations are usually entered into voluntarily, at least from the acquirer's perspective. In the public sector, other parties may be involved in the decision-making process. The freedom that the parties to the combination are able to exercise may influence the economic substance of the combination and hence its classification.
- (e) **Compulsion.** In the public sector, a public sector combination may be imposed by a higher level of government, whether or not that higher level of government controls the parties to the combination for financial reporting purposes. For example, a central government may restructure local government by directing certain municipalities to combine. The IPSASB agreed that compulsion was relevant to the classification of a public sector combination, but considered that information about compulsion would be obtained by having regard to decision-making. Consequently, the IPSASB concluded that it is not necessary to assess this factor independently of the decision-making process.
- (f) **Common control.** In developing the CP, the IPSASB identified the economic differences between public sector combinations that take place under common control and those that take place not under common control (see paragraph BC23 above). The IPSASB agreed that the ability of the controlling entity to specify whether any consideration is transferred is relevant to the classification of the combination, but considered this to be an element of the decision-making process. The fact that the economic resources of the economic entity do not change in a combination under common control, and that any surpluses or deficits would be eliminated on consolidation were seen as relevant to the controlling entity, but not the controlled entity. As the controlled entity will be the reporting entity for the combination, the IPSASB concluded that it is not necessary to assess this factor independently of the decision-making process.
- (g) **Citizens' rights.** In some jurisdictions, citizens may be part of the decision-making process, for example where public sector combinations are subject to the approval of citizens through a referendum. The IPSASB agreed that citizens' rights to accept or reject the combination was relevant to the classification of the combination. However, the IPSASB considered these rights to be rights to participate in the decision-making process. Consequently, the IPSASB concluded that it is not necessary to assess this factor independently of the decision-making process.

BC31. The IPSASB did not consider that the following factors would be helpful in supplementing the concept of control in classifying public sector combinations:

- (a) **Change of sector.** The IPSASB acknowledged that a change of sector would be an indicator of a public sector entity acquiring an operation. However, the IPSASB considered that this change of sector would be a consequence of a change in control rather than a separate factor to be considered. The IPSASB also noted that the classification of institutional units into sectors based on their economic nature of being government units was a feature of GFS that had no equivalent in the IPSASB's literature. This will continue to be a significant difference between macroeconomic statistical reporting and accounting and financial reporting. Consequently, the IPSASB did not consider a change of sector to be a useful factor in classifying public sector combinations.
- (b) **Nature of the jurisdiction.** Some responses to the CP suggested that, in jurisdictions where there is significant interaction or redistribution between the different levels of government, the public sector can be seen as operating as part of a single quasi "group" entity. Such a view could have implications for the classification of public sector combinations. The IPSASB did not consider that from the reporting entity's perspective, the nature of the jurisdiction was relevant to the classification of public sector combinations. A reporting entity could make an assessment of control, consideration and decision-making without reference to a quasi-group entity. The

IPSASB noted that the nature of the jurisdiction may form part of the assessment of the nature of the public sector combination, which an entity may need to consider when the analysis of all other factors has produced inconclusive results or does not provide sufficient evidence to determine the appropriate classification of a public sector combination.

- (c) **Operation of government.** Some respondents to the CP suggested that the operation of government would be relevant to the classification of public sector combinations. Examples given included:
- (i) The existence of a ministerial or other government power enabling the government to direct the entity's governing body to achieve the government's policy objectives;
  - (ii) Ministerial approval is required for operating budgets; and
  - (iii) The government has broad discretion, under existing legislation, to appoint or remove a majority of the members of the governing body of the entity.

The IPSASB concluded that the examples were indicators of control or common control rather than suggesting an independent factor. As such, the IPSASB did not consider that the operation of government was relevant to the classification of public sector combinations.

- (d) **The entity directs public policy and/or engages in non-market activity mainly financed by public resources.** Some respondents to the CP suggested that control should be supplemented by having regard to whether the entity directs public policy and/or engages in non-market activity mainly financed by public resources. Where this was the case, this would suggest an amalgamation. The IPSASB noted that this approach would require the introduction of new concepts into the IPSASB's literature. For example, non-market activity is a GFS concept that the IPSASB has not adopted. The IPSASB did not consider it appropriate to introduce these concepts in ED 60. Consequently, the IPSASB did not consider that this factor was relevant to the classification of public sector combinations.
- (e) **Accountability.** Some respondents suggested that accounting for a public sector combination at fair value provides more information about the effect of that combination, but that this is only useful for accountability purposes where the entity was responsible for the decision to combine. The IPSASB did not consider accountability to be a primary factor in its own right, but acknowledged that the information resulting from the classification of a public sector combination should meet the objectives of financial reporting. In exceptional circumstances, when an analysis of consideration and the decision-making process produces an inconclusive result or does not provide sufficient evidence as to the appropriate classification of a public sector combination, an entity may need to consider other matters, including what information would meet the objectives of financial reporting and satisfy the qualitative characteristics (QCs).

BC32. The IPSASB concluded, therefore, that control should be supplemented by two additional factors—whether consideration was transferred, and the reasons for the presence or absence of consideration; and the decision-making process. These factors are wide ranging, and encompass elements of other factors, as discussed above.

BC33. The IPSASB noted that these factors could be used either to supplement the indicators of control in IPSAS 35, or could be used to supplement the control concept in classifying public sector combinations. The IPSASB debated the merits of these two approaches. The IPSASB noted that using the factors to supplement the indicators of control was likely to result in a classification approach that better satisfied the QC of comparability. However, the IPSASB considered that using the factors to supplement the control concept was likely to produce a classification approach that provided more relevant and faithfully representative information. Using the factors to supplement the control concept was also more likely to address the concerns raised by respondents.

BC34. Respondents to the CP had identified difficulties with distinguishing between acquisitions and amalgamations based solely on control that were unlikely to be fully addressed by further development of the indicators of control. The IPSASB agreed, and concluded that the gaining of control of operations by a party to the combination is an essential element of an acquisition, but is not sufficient in itself to determine whether a combination is an acquisition. Consequently, the IPSASB agreed to develop an approach to classifying public sector combinations that:

- (a) Uses the factors to supplement the concept of control; and

- (b) Considers control in the context of whether a party to the combination gains control of one or more operations as a result of the combination.
- BC35. Having agreed to develop an approach that uses the factors to supplement control, the IPSASB discussed the relative importance to be attached to control and to the other factors in classifying public sector combinations. As part of this discussion, the IPSASB identified the following two approaches:
- (a) **Rebuttable presumption approach.** Under this approach, when one party to the combination gains control of an operation, this creates a rebuttable presumption that the combination is an acquisition. This approach gives a strong weighting to the gaining of control, and the analysis of the other factors is focused on whether there is sufficient evidence to rebut this presumption.
  - (b) **Individual weighting approach.** Under this approach, the weightings given to the gaining of control, consideration and decision-making are a matter for professional judgment based on the individual circumstances of the combination. Preparers would identify which (if any) factors indicate an acquisition and which (if any) factors indicate an amalgamation. Where indicators of both an acquisition and an amalgamation are present, the weighting given to the respective factors by preparers using professional judgment would determine the classification.
- BC36. The IPSASB noted that the rebuttable presumption approach provided greater clarity, and better satisfied the QC of comparability. The individual weighting approach was likely to be more subjective in practice. However, the IPSASB acknowledged that the individual weighting approach would enable practitioners to better reflect the economic substance of the combination, and might better meet the QCs of relevance and faithful representation.
- BC37. Control was seen by most members as more important in determining the classification than the other factors, and the rebuttable presumption approach reflected this. Consequently, the IPSASB agreed to develop the rebuttable presumption approach.
- BC38. In coming to this decision the IPSASB noted that an approach that considered other factors as supplementing control (which better satisfies the QCs of relevance and faithful representation at the expense of comparability) while at the same time incorporating a rebuttable presumption that one party to a combination gaining control of operations gives rise to an acquisition (which better satisfies the QC of comparability at the expense of relevance and faithful representation) is likely to produce an appropriate balance between the QCs.
- BC39. The IPSASB also considered the possibility that, in rare circumstances, neither the consideration nor the decision-making indicators would be sufficient to rebut the presumption that a public sector combination was an acquisition even though this classification did not reflect the economic substance of the combination. The IPSASB agreed to require consideration of the economic substance of the combination when determining whether the presumption should be rebutted. To assist preparers in this determination, ED 60 also required, in these rare circumstances, an assessment as to which classification produces information that best satisfies the objectives of financial reporting and the QCs.
- BC40. The IPSASB considered that the most common circumstances in which a public sector combination would be considered an acquisition are:
- (a) One party to the combination gains control of an operation and pays consideration that is intended to compensate those with an entitlement to the net assets of the transferred operation for giving up that entitlement.
  - (b) One party to the combination gains control of an operation from outside the public sector without paying consideration to compensate those with an entitlement to the net assets of the transferred operations.
  - (c) One party to the combination gains control of an operation from outside the public sector by imposing the combination on the other party.
  - (d) One party to the combination gains control of an operation from a separate government.

The IPSASB noted that, except in exceptional cases, the classification approach adopted in ED 60 would result in such combinations being classified as acquisitions. This provided reassurance to the IPSASB that the approach adopted was appropriate.



*Responses to ED 60*

- BC41. The IPSASB considered the responses to ED 60. The IPSASB noted that there was substantial support for the overall approach to classifying public sector combinations in the ED.
- BC42. Respondents did, however, identify areas where they considered the approach could be improved. The main issues identified were:
- (a) Having a rebuttable presumption that was expected to be rebutted significantly more frequently than not was confusing;
  - (b) The approach was seen as giving too much emphasis to control, with some stakeholders interpreting the ED as requiring the use of the acquisition method in most cases where one party to the combination gained control of operations; and
  - (c) In many jurisdictions, it will be easier to determine the economic substance of a public sector combination by reference to the indicators (consideration and decision making) than by reference to whether one party to the combination gained control of operations.
- BC43. The IPSASB acknowledged these concerns. The IPSASB accepted that rebuttable presumptions are generally expected to be rebutted infrequently, and that the use of this term with an expectation that it would be frequently rebutted may be confusing for preparers. This confusion could result in a preparer classifying a public sector combination as an acquisition when this was not the IPSASB's intention.
- BC44. The IPSASB considered that the potential confusion as to how the rebuttable presumption was to be interpreted might explain the concerns of some stakeholders that the acquisition method would be used inappropriately. The IPSASB did not intend that the approach in the ED would require the use of the acquisition method in most cases where one party to the combination gained control of operations. The IPSASB considered that acquisitions would arise in limited circumstances, as can be seen from the list in paragraph BC40 above.
- BC45. The IPSASB accepted that, in many jurisdictions, the economic substance of a public sector combination could be more readily determined by reference to the indicators, in particular whether a combination occurred under common control. However, the IPSASB noted that this was not the case for all jurisdictions. The IPSASB noted that control remained a significant factor; in particular, an acquisition can only occur when a party to the combination gains control of one or more operations. The IPSASB also noted that the approach in ED 60 provided a suitable decision framework for ensuring all relevant factors were considered.
- BC46. Consequently, the IPSASB agreed to reconsider the way the classification approach is expressed to address these concerns, without changing the substance of the approach. The rebuttable presumption and reference to control was intended to be the first step in the process of determining a classification based on the economic substance of the combination. In creating this first step, the IPSASB did not intend that, once it has been established that one party has gained control, control should be given greater weight than consideration and decision making in determining the economic substance of the combination. The IPSASB accepted that the reference in BC35(a) to the approach giving a strong weighting to the gaining of control could be misleading. Control remains important, as its absence eliminates the possibility of an acquisition, but its significance in determining the economic substance of a particular combination where one party has gained control is a matter of professional judgment. The IPSASB remains of the view that the classification approach in ED 60 was appropriate, and the changes introduced in this Standard are intended to provide greater clarity as to how the approach should be applied. These changes are not intended to produce different classifications from ED 60.

*Comparison with IFRS 3*

- BC47. This Standard is not converged with IFRS 3. IFRS 3 considers all business combinations to be acquisitions, whereas this Standard provides for both amalgamations and acquisitions. The IPSASB considers this difference to be appropriate, for the following reasons:
- (a) In developing IFRS 3, the IASB concluded that 'true mergers' or 'mergers of equals' in which none of the combining entities obtains control of the others are so rare as to be virtually non-existent. However, in the public sector, such combinations are common. Developing a Standard that did not address amalgamations would not meet the needs of the users of public sector GPFs.

- (b) IFRS 3 assumes that it is always possible to identify the acquirer, as the businesses to which IFRS 3 applies will always have owners. In the public sector, there may be no quantifiable ownership interests in a public sector entity, which can make it impossible to identify an acquirer. Developing a Standard that does not recognize this situation would not meet the needs of the users of public sector GPFs.

### Accounting for Amalgamations (paragraphs 15–57)

#### *Reasons for adopting the modified pooling of interests method of accounting for amalgamations*

- BC48. In developing the CP, the IPSASB identified three methods of accounting for public sector combinations that have either been applied in practice, or discussed. These are:
- (a) The acquisition method;
  - (b) The pooling of interests method, including a possible modification to this method; and
  - (c) The fresh start method.
- BC49. The acquisition method (which is applied by IFRS 3) requires that an acquirer is identified for all combinations. The IPSASB had already concluded that it may not be possible to identify an acquirer for all public sector combinations, and that any combination in which an acquirer could not be identified would be classified as an amalgamation. The IPSASB therefore concluded that the acquisition method of accounting would not be appropriate for amalgamations.
- BC50. The pooling of interests method of accounting was previously used in IAS 22, *Business Combinations* (the predecessor standard to IFRS 3). It was intended for application to a combination in which an acquirer cannot be identified. The pooling of interests method of accounting was previously used by many jurisdictions as the basis for merger accounting or amalgamation accounting. It continues to be used by many entities when accounting for combinations under common control (which are outside the scope of IFRS 3).
- BC51. The pooling of interests method accounts for the combining operations as though they were continuing as before, although now jointly owned and managed. The financial statement items of the combining operations for the period in which the combination occurs, and for any comparative periods disclosed, are included in the financial statements of the resulting entity as if they had been combined from the beginning of the earliest period presented. In other words, the recognition point is the beginning of the earliest period presented, and, consequently, comparative information is restated.
- BC52. The IPSASB noted that some are of the view that the requirement to restate comparative information might be onerous and unnecessary. In the CP, the IPSASB consulted on a variation of the pooling of interests method of accounting, described as the modified pooling of interests method of accounting. Under the modified pooling of interests method, the resulting entity combines the items in the statement of financial position as at the date of the amalgamation.
- BC53. The third method the IPSASB discussed in the CP was the fresh start method of accounting. In contrast to the pooling of interests method of accounting, the premise of the fresh start method is that the resulting entity is a new entity (irrespective of whether a new entity is formed) and therefore its history commences on that date. The modified pooling of interests method has a similar effect in practice.
- BC54. The fresh start method requires recognition of all of the identifiable assets and liabilities of all the combining operations at fair value as at the date of the combination in the financial statements of the resulting entity. This includes recognizing identifiable assets and liabilities that were not previously recognized by the combining operations. In other words, the fresh start method uses the same recognition and measurement basis as the acquisition method, but applies it to all of the combining operations rather than just acquired operations.
- BC55. In developing the CP, the IPSASB came to the conclusion that the pooling of interests method of accounting, the modified pooling of interests method of accounting and the fresh start method of accounting all provided a possible basis for accounting for amalgamations.
- BC56. The IPSASB noted that the future cash flows and service potential of the resulting entity will generally be the same regardless of which method is used to account for the amalgamation. However, the presentation of the financial performance and financial position of the resulting entity differs

significantly depending on the method applied. If preparers are given a free choice of method, this would reduce comparability between entities and over time.

- BC57. Supporters of the pooling or modified pooling of interests method of accounting for amalgamations considered that these methods satisfy users' needs:

- (a) For information for decision-making purposes; and
- (b) To assess the accountability of the resulting entity for its use of resources.

This is because users of public sector entities' GPFSs use the information to assess how financial resources have been allocated and the financial condition of an entity. This information can be obtained by applying the pooling or modified pooling of interests methods of accounting.

- BC58. These methods are seen as satisfying the QCs of relevance and faithful representation, because they reflect the amounts recognized in the financial statements of the combining operations before the amalgamation. The subsequent performance of the resulting entity, and its accountability for the management of those resources, can be assessed on the same basis as was used to assess accountability before the amalgamation.

- BC59. The pooling or modified pooling of interests methods of accounting are seen as generally the least costly to apply, because they:

- (a) Use the existing carrying amounts of the assets, liabilities, and net assets/equity of the combining operations; and
- (b) Do not require identifying, measuring, and recognizing assets or liabilities not previously recognized before the amalgamation.

- BC60. Supporters of the modified pooling of interests method of accounting consider it to be superior to the pooling of interests method because it portrays the amalgamation as it actually is. This is because it recognizes the assets and liabilities of the combining operations at the date of the amalgamation. Supporters consider this to be a faithful representation of the amalgamation.

- BC61. Those who support the use of the modified pooling of interests method acknowledge that the history of the combining operations may help in assessing the performance of the resulting entity. In debating the merits of the different methods, the IPSASB acknowledged that adopting the modified pooling of interests method of accounting without addressing users' needs for historical information may not satisfy the objectives of financial reporting.

- BC62. Others consider that the fresh start method of accounting is conceptually superior to both the pooling of interests method of accounting and its modified version, because the resulting entity is held accountable for the current value of the resources of the combining operations. It also provides more complete information of an amalgamation, because it recognizes the identifiable assets and liabilities of the combining operations, regardless of whether they were recognized prior to the amalgamation.

- BC63. Supporters of the fresh start method of accounting consider that it satisfies users' needs:

- (a) For information for decision-making purposes; and
- (b) To assess the accountability of the resulting entity for its use of resources.

This is because it enables users to better assess the financial condition of the entity and how the financial resources have been allocated.

- BC64. Supporters of the fresh start method of accounting consider that this method is, to a large extent, an extension of the use of fair value in the acquisition method of accounting. Consequently, they argue that if the acquisition method is adopted for acquisitions, there is no reason not to adopt similar accounting for amalgamations.

- BC65. In developing the CP, the IPSASB came to the view that the modified pooling of interests method of accounting is the appropriate method to apply, because users' are able to assess the performance and accountability of the resulting entity without the entity having to remeasure its assets and liabilities. Furthermore, it recognizes the amalgamation on the date it takes place. The IPSASB noted that IPSASs permit revaluation to fair value subsequent to initial recognition if a resulting entity considers that this approach would provide more relevant information to users.

- BC66. Respondents to the CP generally supported the IPSASB's view that the modified pooling of interests method of accounting is the appropriate method to apply to amalgamations. The IPSASB reconsidered the methods in developing ED 60, and identified no reason to change its previously stated view. The IPSASB therefore agreed that the modified pooling of interests method of accounting should be adopted for amalgamations in ED 60. In coming to this decision, the IPSASB agreed that the modified pooling of interests method of accounting should include appropriate disclosures to ensure that the users of public sector entities' GPFs had access to the historical information they need.
- BC67. Respondents to ED 60 generally agreed that the modified pooling of interests method of accounting is the appropriate method to apply to amalgamations. However, some respondents considered that the pooling of interests method of accounting provided better information, and only supported the modified pooling of interests method for cost/benefit reasons. These respondents considered that, in some circumstances, the benefits of providing prior period information would outweigh the cost of so doing. The IPSASB accepted this view, and agreed that resulting entities should be permitted, but not required, to present prior period information. The IPSASB decided that prior period information should not be restated, as doing so would require the use of a different recognition point, which would reduce comparability.

*Exceptions to the principle that assets and liabilities are recognized and measured at their previous carrying amount*

- BC68. The modified pooling of interests method of accounting requires the resulting entity to recognize and measure the assets and liabilities of the combining operations at their previous carrying amounts, subject to the requirement to adjust the carrying amounts to conform to the resulting entity's accounting policies. The effects of all transactions between the combining operations, whether occurring before or after the amalgamation date, are eliminated in preparing the financial statements of the resulting entity.
- BC69. The IPSASB considered the circumstances in which the application of these principles would not be appropriate. The IPSASB identified three circumstances in which an exception to the recognition and/or measurement principles would be appropriate:
- (a) **Licenses and similar rights previously granted by one combining operation to another combining operation.** A license or similar right may have been granted by one combining operation to another combining operation and recognized as an intangible asset by the recipient. Applying the general principles would require this transaction to be eliminated. However, the IPSASB considered that, in granting the license or similar right, the recognition criteria for an intangible asset are met. Where internally generated intangible assets are not recognized, this is because of the problems in identifying whether and when there is an identifiable asset that will generate expected future economic benefits or service potential; and in determining the cost of the asset reliably. Once a license or similar right has been granted to a recipient, this demonstrates that there is an identifiable asset that will generate future economic benefits or service potential. Similarly, the transaction will establish a cost for the asset. Consequently, the recognition criteria for an intangible asset are met. Because of this, the asset is not eliminated when combining operations that have granted and received the license or similar right are part of an amalgamation. The situation is similar to that where a tangible asset is sold by one combining operation to another combining operation. Eliminating the effect of the sale does not eliminate the tangible asset itself, as the asset was previously recognized by the seller. In the case of a license or similar right, eliminating the transaction does not eliminate the intangible asset, as the transaction provides sufficient evidence of the existence of the intangible asset, such that the grantor would itself recognize that intangible asset. The IPSASB noted that in some cases where a combining operation gains control of other operations, the right might be considered as a reacquired right. The IPSASB did not consider that this would warrant a different accounting treatment, and noted that reacquired rights are recognized as intangible assets under the acquisition method. For these reasons, the IPSASB concluded that the asset recognized in respect of a license or similar right previously granted by one combining operation to another should not be eliminated.
  - (b) **Income taxes.** In the public sector, amalgamations, especially those imposed by a higher level of government, may include tax forgiveness as part of the terms and conditions of the amalgamation. The IPSASB agreed that the resulting entity should recognize any tax items that exist following the amalgamation rather than those that existed prior to the amalgamation. Having considered comments by respondents to ED 60, the IPSASB agreed that there may be

cases where any tax forgiveness arises subsequent to the amalgamation, rather than as part of the terms and conditions of the amalgamation. The IPSASB agreed to include provisions dealing with both cases in IPSAS 40.

- (c) **Employee benefits.** The IPSASB noted that the assets and liabilities required to be recognized by IPSAS 39, *Employee Benefits*, in respect of a post-employment benefit plan following an amalgamation might differ from the combined carrying amounts of the combining operations' equivalent amounts. As an example, an amalgamation involves five combining operations who are the only participants in a multi-employer defined benefit plan. Prior to the amalgamation, the combining operations have insufficient information to determine each combining operation's proportionate share of the defined benefit obligation, plan assets, and cost associated with the plan. As a result, the combining operations account for the plan as if it is a defined contribution plan. Following the amalgamation, the resulting entity is the only participant in the plan, and is able to determine its defined benefit obligation, plan assets, and cost associated with the plan. It therefore accounts for the plan as a defined benefit plan from the date of the amalgamation. The IPSASB agreed that the resulting entity's opening statement of financial position should include the assets and liabilities measured in accordance with IPSAS 39.

*Recognizing and measuring components of net assets/equity arising as a result of an amalgamation*

- BC70. In developing ED 60, the IPSASB noted that a residual amount might arise as a result of an amalgamation. The IPSASB considered how this should be recognized and measured. The IPSASB agreed that the residual amount does not reflect the financial performance of the resulting entity, and concluded that the residual amount should be recognized in the resulting entity's opening statement of financial position.
- BC71. The IPSASB considered the nature of the residual amount. The IPSASB considered that, for amalgamations not under common control, the residual amount represents the past financial performance of the combining operations not included in their transferred net assets/equity. The IPSASB agreed that the residual amount should be included in the resulting entity's opening net assets/equity where the amalgamation takes place not under common control.
- BC72. The IPSASB considered that, for amalgamations under common control, the residual amount represents the financial consequences of decisions made by the controlling entity in setting or accepting the terms of the amalgamation. Consequently, the IPSASB agreed that the residual amount should be treated as an ownership contribution or ownership distribution where the amalgamation takes place under common control.
- BC73. The IPSASB considered the items that should be included in the residual amount. The IPSASB noted that the modified pooling of interests method of accounting usually recognizes an amalgamation as giving rise to, in substance, a new entity on the date the amalgamation takes place. As the new entity would not have generated other components of net assets/equity such as accumulated surplus or deficit, or revaluation surplus, all items within net assets/equity would be included as part of the residual amount.
- BC74. The IPSASB considered that this approach best reflects the conceptual basis of an amalgamation and agreed that all items within net assets/equity at the amalgamation date should be considered to be part of the residual amount. In coming to this view, the IPSASB accepted that this approach may have consequences for some entities. For example, because the residual amount would include any previously recognized revaluation surplus, any future revaluation decreases are more likely to be recognized in surplus or deficit. This is because the previously recognized revaluation surplus would no longer be available to absorb future revaluation decreases.
- BC75. Another consequence relates to amalgamations that take place under common control. The resulting entity would recognize a residual amount but the controlling entity would continue to recognize the previous components of net assets/equity in its consolidated financial statements, giving rise to ongoing consolidation adjustments. The IPSASB did not consider that these consequences outweighed the benefits of adopting the conceptual approach.

## Responses to ED 60

- BC76. Although the majority of respondents to ED 60 supported the IPSASB's approach to the residual amount, a significant minority did not. The main reasons respondents gave for not supporting the proposed treatment of the residual amount were as follows:
- (a) Retaining existing reserves better represents the combination, is more transparent and better meets users' needs;
  - (b) The proposals will result in reliable information on the revaluation reserve being discarded;
  - (c) For amalgamations under common control, the combining entities may effectively be continuing as one entity rather than as two or more separate entities, as opposed to being a new entity;
  - (d) Reporting subsequent revaluation losses as an expense risks misrepresenting financial performance in future years;
  - (e) The proposals will produce ongoing consolidation adjustments where the amalgamation takes place under common control, and the need to prepare these adjustments outweighed the benefits of recognizing a single residual amount; and
  - (f) The proposals will impact on a wide range of reserves, including those relating to employee benefits, hedging and reserves restricted by legislation, which would be inconsistent with ED 60's requirement that the existing classifications and designations are maintained.
- BC77. The IPSASB was persuaded by some of the reasons provided by respondents. In particular the IPSASB acknowledged that the proposals in ED 60 might be internally inconsistent.
- BC78. The IPSASB therefore reconsidered the proposal to require all amounts recognized in net assets/equity to be recognized in the residual amount.
- BC79. The IPSASB concluded that the most appropriate presentation of net assets/equity would depend on the circumstances of the amalgamation. In an amalgamation not under common control, and where there were no reserves such as those referred to in paragraph BC76(f) above, presenting a single opening balance in net assets/equity could provide faithfully representative information. In an amalgamation under common control, and with reserves such as those referred to in paragraph BC76(f) above, presenting a single opening balance in net assets/equity is unlikely to provide faithfully representative information. In these circumstances, presenting separate components of net assets/equity will provide more relevant and useful information.
- BC80. Consequently, the IPSASB decided not to specify which components of net assets/equity should be presented, as preparers will be in the best position to judge the most appropriate treatment. The IPSASB agreed to amend the requirements accordingly.

*Measurement period*

- BC81. IFRS 3 permits acquirers a period of one year after the acquisition date to complete the accounting for the acquisition. This is to allow the acquirer sufficient time to obtain information to determine the fair value of an acquired operation's assets and liabilities.
- BC82. The IPSASB considered whether such a period was required when accounting for an amalgamation. The modified pooling of interests method does not require assets and liabilities to be restated to fair value at the amalgamation date. However, the IPSASB noted that the combining operations may have different accounting policies, which could result in some assets and liabilities being required to be restated to conform to the resulting entity's accounting policies. For example, the resulting entity may adopt an accounting policy of revaluing certain assets such as property, plant and equipment. If one or more combining operations had previously adopted an accounting policy of measuring such assets at cost, the practical effect of determining the carrying amount of those assets under the revaluation model would be similar to that of determining their fair value. For this reason, the IPSASB agreed that it was appropriate to permit a resulting entity time to obtain the information needed to restate assets and liabilities to conform to its accounting policies. The IPSASB agreed that a period of one year was appropriate.

*Combining operations that have not previously adopted accrual basis IPSASs*

- BC83. In developing this Standard, the IPSASB considered whether it was necessary to include specific provisions to address the situation where one or more combining operations had not previously adopted accrual basis IPSASs. For example, one public sector entity that has previously applied accrual basis IPSASs may be amalgamated with a second public sector entity that has previously applied an alternative accrual basis of accounting. In such circumstances, recognizing and measuring the second public sector entity's assets and liabilities at their carrying amount may not be consistent with the requirements of accrual basis IPSASs.
- BC84. The IPSASB concluded that no separate provisions were required in this Standard. Paragraph 27 of IPSAS 40 requires the resulting entity to adjust the carrying amounts of the identifiable assets and liabilities of the combining operations where required to conform to the resulting entity's accounting policies. The IPSASB considered this requirement to be sufficient to address most circumstances where one or more combining operations had not previously adopted accrual basis IPSASs.
- BC85. The IPSASB came to the view that where adjusting the carrying amounts to conform to the resulting entity's accounting policies was insufficient to achieve compliance with accrual basis IPSASs, the resulting entity would be a first-time adopter of accrual basis IPSASs. This could occur where one or more combining operations had previously adopted the cash basis of accounting and had, therefore, not previously recognized certain assets and liabilities. In these circumstances, the resulting entity would apply IPSAS 33, *First-time Adoption of Accrual Basis International Public Sector Accounting Standards (IPSASs)* in preparing its first post-combination financial statements.

**Accounting for acquisitions (paragraphs 58–125)***Reasons for adopting the acquisition method of accounting for acquisitions*

- BC86. In developing the CP, the IPSASB did not reach a conclusion as to “whether the use of fair value as the measurement basis, is appropriate for some or all acquisitions in the public sector. This is because the most prevalent types of acquisition occur where operations are acquired for the achievement of objectives relating to the delivery of goods and/or services, instead of generating economic benefits to return to equity holders. Moreover, many acquisitions do not include the transfer of consideration. Some consider that these types of acquisitions are different in nature from business combinations as identified in IFRS 3, because the concept of acquiring an operation directly in exchange for the transfer of consideration is missing.” Respondents to the CP generally supported the use of fair value for acquisitions in which consideration was transferred. For acquisitions in which no consideration was transferred, there was broadly equal support for fair value measurement and measurement at carrying amount.
- BC87. The arguments developed in the CP reflected the classification approach in the CP. In the CP, the IPSASB proposed that the gaining of control was the sole definitive criterion for distinguishing an amalgamation from an acquisition. The IPSASB has subsequently decided to supplement the gaining of control with two other factors, consideration and decision-making. The IPSASB considers that this will result in fewer public sector combinations being classified as acquisitions than under the approach in the CP. Those public sector combinations that are classified as acquisitions will be similar in nature to the business combinations addressed by IFRS 3.
- BC88. Having regard to the revised classification approach that it had agreed to adopt, the IPSASB reconsidered which accounting method would be appropriate for acquisitions. The IPSASB concluded that the acquisition method was appropriate, and agreed to adopt the acquisition method as set out in IFRS 3 as the accounting method for acquisitions in this Standard. This approach was supported by respondents to ED 60.

*Differences to the accounting treatments in IFRS 3*

- BC89. IFRS 3 includes accounting treatments that are based on other IFRS Standards for which there is no equivalent IPSAS, for example income taxes and share-based payment. The IPSASB agreed not to include the detailed requirements specified in IFRS 3, but to include references to the relevant international or national accounting standard dealing with the issue.
- BC90. The IPSASB considered whether any additional guidance to that provided by IFRS 3 was required. The IPSASB noted that acquisitions in the public sector may include assets and liabilities arising from non-

exchange transactions that are not addressed in IFRS 3. Consequently, the IPSASB agreed to include additional guidance on the following non-exchange items:

- (a) Tax forgiveness; and
- (b) The subsequent measurement of transfers, concessionary loans and similar benefits received by a combining operation on the basis of criteria that may change as a result of an acquisition.

BC91. The IPSASB considered comments from respondents to ED 60 regarding the acquisition method. As a result, the IPSASB agreed to make minor changes to the requirements:

The tax forgiveness requirements have been amended to allow for those cases where tax forgiveness occurs subsequent to the acquisition as well as where it forms part of the terms of the acquisition.

The IPSASB considered whether any additional exemptions to the recognition and measurement principles or any additional guidance on the acquisition method were required. The IPSASB concluded that no further provisions were necessary, as the Board considered that the provisions in this Standard or in other IPSASs were already sufficiently clear.

*Acquired operations that have not previously adopted accrual basis IPSASs*

BC92. In developing this Standard, the IPSASB considered whether it was necessary to include specific provisions to address the situation where one or more acquired operations had not previously adopted accrual basis IPSASs. The IPSASB concluded that no separate provisions were required in this Standard. Paragraph 64 of IPSAS 40 requires an acquirer to recognize the identifiable assets acquired, the liabilities assumed and any non-controlling interest in an acquired operation. Paragraph 72 of the Standard requires the acquirer to measure the assets and liabilities acquired at their acquisition-date fair values. Consequently, the acquirer will measure all assets and liabilities in accordance with accrual basis IPSASs, irrespective of the accounting basis previously adopted by an acquired operation.

*Fair value cannot be determined*

BC93. Respondents to ED 60 commented that, in exceptional circumstances, it may be impracticable for an acquirer to determine the fair value of an item and suggested that the use of the item's previous carrying amount may be an appropriate alternative. The IPSASB considered this suggestion but concluded that using carrying amount may not be appropriate in all instances, particularly if the acquired operation does not apply accrual based IPSASs. The IPSASB agreed that entities should apply the existing requirements in IPSASs. In particular, the IPSASB noted that, in accordance with IPSAS 3, *Accounting Policies, Changes in Accounting Estimates and Errors*, applying a requirement is impracticable when the entity cannot apply it after making every reasonable effort to do so. IPSAS 3 provides additional guidance. In such cases, the acquirer would measure the item as of the acquisition date in a manner that is consistent with other IPSASs and the acquirer's accounting policies, and make the disclosures required by other IPSASs. The IPSASB considered that it would be appropriate to measure the item at its previous carrying amount only where that carrying amount is consistent with other IPSASs and the acquirer's accounting policies.



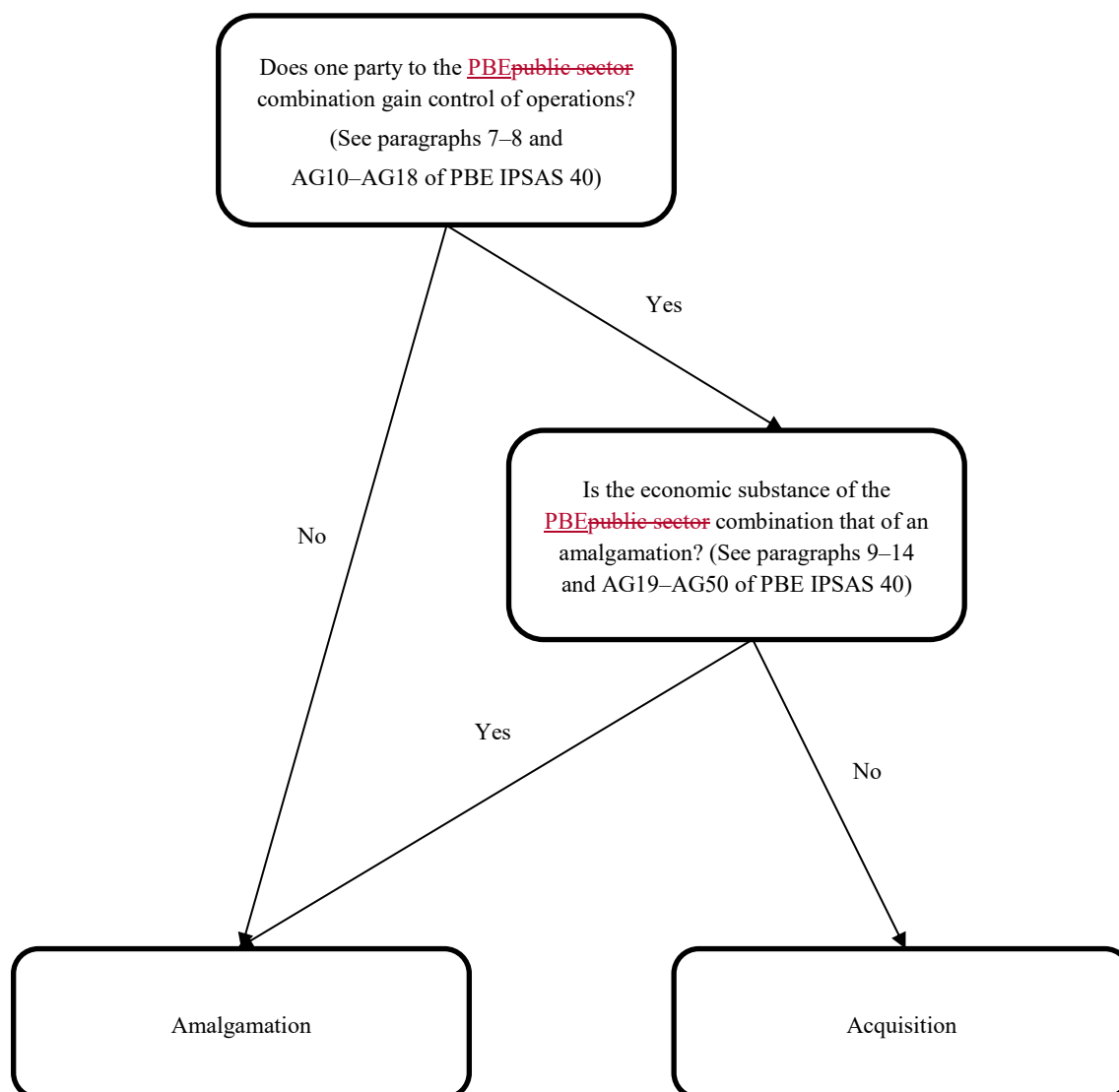
## Implementation Guidance

*This guidance accompanies, but is not part of, PBE IPSAS 40*

IG1. The purpose of this Implementation Guidance is to illustrate certain aspects of the requirements of PBE IPSAS 40.

### Classification of PBE Combinations

IG2. The diagram below summarises the process established by PBE IPSAS 40 for classifying PBE combinations.



## Illustrative Examples

*These examples accompany, but are not part of, PBE IPSAS 40*

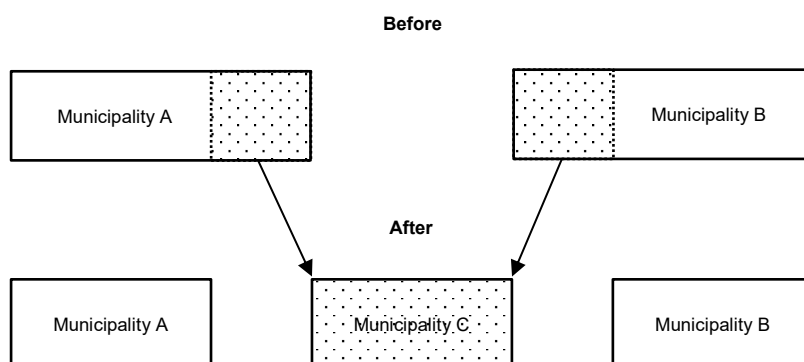
### Classification of ~~PBEpublic sector~~ Combinations

*Illustrating the consequences of applying paragraphs 7–14 and AG10–AG50 of PBE IPSAS 40*

- IE1. The following scenarios illustrate the process for classifying ~~PBEpublic sector~~ combinations. These scenarios portray hypothetical situations. Although some aspects of the scenarios may be present in actual fact patterns, all facts and circumstances of a particular fact pattern would need to be evaluated when applying PBE IPSAS 40.
- IE2. Each scenario is illustrated by a diagram. Where a ~~PBEpublic sector~~ combination involves operations which form part of an economic entity, but not the whole economic entity, the operations that are involved in the combination, and the entity that is formed by the combination, are shaded in the diagram. Where more than one reporting entity is included in an economic entity, the boundary of the economic entity is shown by a dotted line.

#### *Scenario 1: Reorganisation of Local Government by Rearranging Territorial Boundaries*

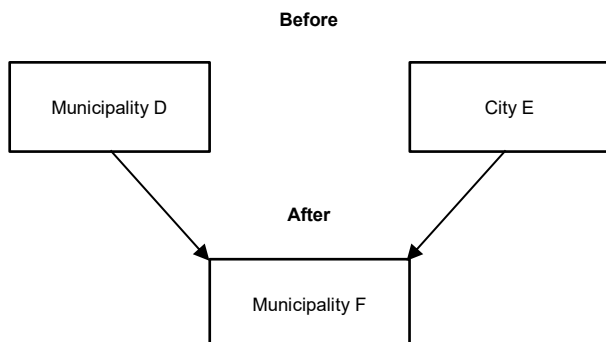
- IE3. The following diagram illustrates the creation of a new municipality by combining some operations from two existing municipalities.



- IE4. In this scenario, the territorial boundaries of two existing municipalities, Municipality A and Municipality B, are redrawn by Parliament through legislation; neither Parliament nor Central Government controls Municipality A or Municipality B. Responsibility for part of each municipality's former territory is transferred to a new municipality, Municipality C. Operations in respect of the transferred territory are combined to form Municipality C. A ~~PBEpublic sector~~ combination occurs.
- IE5. Municipality A and Municipality B remain otherwise unchanged and retain their governing bodies. A new governing body (unrelated to the governing bodies of Municipality A and Municipality B) is elected for Municipality C to manage the operations that are transferred from the other municipalities.
- IE6. The creation of Municipality C is a ~~PBEpublic sector~~ combination. In determining whether this should be classified as an amalgamation or an acquisition, the first question to consider is whether one of the parties to the combination has gained control of operations as a result of the combination.
- IE7. Municipality C has a newly elected governing body, unrelated to the governing bodies of Municipality A and Municipality B. Neither Municipality A nor Municipality B has power over the Municipality C. Neither do they have exposure, or rights, to variable benefits from any involvement with Municipality C.
- IE8. Neither Municipality A nor Municipality B have gained control over Municipality C as a result of the ~~PBEpublic sector~~ combination. Consequently the combination is classified as an amalgamation.

*Scenario 2: Reorganisation of Local Government by Combining Municipalities into a New Legal Entity*

- IE9. The following diagram illustrates the creation of a new municipality by combining all of the operations of two existing municipalities into a new legal entity.



- IE10. In this scenario, a ~~PBE public sector~~ combination occurs in which Municipality F is formed to combine the operations (and the related assets, liabilities and components of net assets/equity) of Municipality D and City E. Prior to the combination, Municipality D and City E are not under common control. The combination is imposed by the provincial government (a third party) through legislation. The provincial government has the legal power to direct the two entities to combine, through legislation, even though it does not control them.
- IE11. The legislation that creates Municipality F provides for the formation of a new governing body with no links to Municipality D or City E. Municipality D and City E have no role in determining the terms of the combination. After the combination, Municipality D and City E cease to exist.
- IE12. The creation of Municipality F is a ~~PBE public sector~~ combination. In determining whether this should be classified as an amalgamation or an acquisition, the first question to consider is whether one of the parties to the combination has gained control of operations as a result of the combination.
- IE13. Municipality F has a newly formed governing body, unrelated to the governing bodies of Municipality D and City E. Neither Municipality D nor City E has power over Municipality F. Neither do they have exposure, or rights, to variable benefits from any involvement with Municipality F.
- IE14. Neither Municipality D nor City E have gained control over Municipality F as a result of the ~~PBE public sector~~ combination. Consequently the combination is classified as an amalgamation.

**Scenario 2: Variation**

- IE15. In scenario 2, the legislation that creates Municipality F provides for the formation of a new governing body with no links to Municipality D or City E. In this variation, the legislation that creates Municipality F provides for the governing body of Municipality D to become the governing body of Municipality F.
- IE16. This suggests that as part of the ~~PBE public sector~~ combination that creates Municipality F, Municipality D is gaining control of the operations of City E. However, the assessment as to whether Municipality D is gaining control is based on the substance of the combination, not its legal form. In preparing its first financial statements, Municipality F considers the guidance in paragraphs 7–8 and AG10–AG18 of ~~IPSAS 40~~ PBE IPSAS 40.
- IE17. In this variation, it is assumed that the legislation that provides for the governing body of Municipality D to become the governing body of Municipality F results in Municipality D gaining:
- Power over the operations of City E;
  - Exposure, or rights, to variable benefits from its involvement with those operations; and
  - The ability to use its power over those operations to affect the nature or amount of the benefits from its involvement with those operations.
- IE18. Municipality F concludes that, as a result of the ~~PBE public sector~~ combination, Municipality D has gained control of City E. Municipality F considers the guidance in paragraphs 9–14 and AG19–AG50

of PBE IPSAS 40 in determining whether the economic substance of the combination is that of an amalgamation.

- IE19. ~~[Not used] In considering the economic substance of the public sector combination, Municipality F notes that the combination does not result in a controlling entity/controlled entity relationship between Municipality D and City E. This is consistent with both an amalgamation and an acquisition. Municipality F also notes that Municipality D obtains access to economic benefits or service potential that are similar to those that could have been obtained by mutual agreement; this may suggest that the economic substance of the combination is that of an acquisition, but is not conclusive.~~

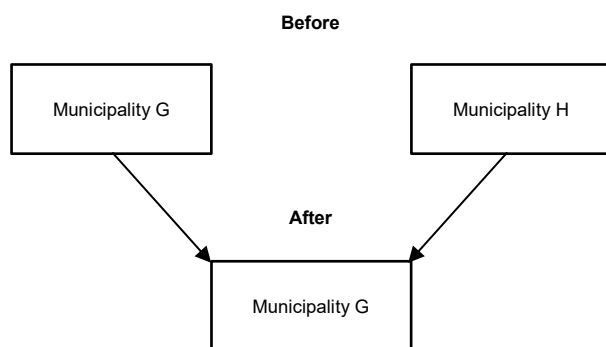
Agenda item 7.1 reference: Illustrative examples (paras 39–41)

- IE20. In considering the indicators relating to consideration, Municipality F notes that the ~~public sector~~PBE combination does not include the payment of consideration ~~because there is no party with an entitlement to the net assets of City E (i.e., there are no former owners of City E with quantifiable ownership interests).~~ This suggests that the economic substance of the combination is that of an amalgamation.
- IE21. In considering the indicators relating to the decision-making process, Municipality F notes that the ~~public sector~~PBE combination was imposed by the provincial government (a third party) and that Municipality D and City E had no role in determining the terms of the combination. This may suggest that the economic substance of the combination is that of an amalgamation.
- IE22. ~~Taking these factors together, On balance these factors suggest Municipality F considers that the public sector~~PBE combination should be classified as an amalgamation. ~~In coming to this decision, Municipality F considers the absence of consideration because there is no party with an entitlement to the net assets of an operation to be the most significant factor in determining the economic substance of the combination.~~

Agenda item 7.1 reference: Indicator in paragraph 12(c) (paras 10–17)

*Scenario 3: Reorganisation of Local Government by Combining Municipalities into an Existing Legal Entity*

- IE23. The following diagram illustrates the combining of all of the operations of two existing municipalities into an existing legal entity.



- IE24. In this scenario, a ~~PBE~~public-sector combination occurs in which the operations of Municipality G and Municipality H (and their related assets, liabilities and components of net assets/equity) are combined into the legal entity of Municipality G. Prior to the combination, Municipality G and Municipality H are not under common control. The combination is imposed by Central Government (a third party) through legislation. Central Government has the legal power to direct the two entities to combine, through legislation, even though it does not control them.
- IE25. The legislation that effects the combination provides for the governing body of Municipality G to continue as the governing body of the combined entity. Municipality G and Municipality H have no role in determining the terms of the combination. After the ~~PBE~~public-sector combination, Municipality H ceases to exist.
- IE26. These facts suggest that as part of the ~~PBE~~public-sector combination, Municipality G is gaining control of the operations of Municipality H. However, the assessment as to whether Municipality G is gaining control is based on the substance of the combination, not its legal form. Municipality G considers the

guidance in paragraphs 7–8 and AG10–AG18 of ~~IPSAS 40~~PBE IPSAS 40 in determining whether to classify the combination as an amalgamation or an acquisition.

- IE27. In this scenario, it is assumed that the legislation that provides for the governing body of Municipality G to continue as the governing body of combined entity results in Municipality G gaining:
- (a) Power over the operations of Municipality H;
  - (b) Exposure, or rights, to variable benefits from its involvement with those operations; and
  - (c) The ability to use its power over those operations to affect the nature or amount of the benefits from its involvement with those operations.
- IE28. Municipality G concludes that, as a result of the ~~PBE public-sector~~ combination, it has gained control of Municipality H. Municipality G considers the guidance in paragraphs 9–14 and AG19–AG50 of PBE IPSAS 40 in determining whether the economic substance of the combination is that of an amalgamation.
- IE29. ~~[Not used] In considering the economic substance of the public-sector combination, Municipality G notes that the combination does not result in a controlling entity/controlled entity relationship between Municipality G and Municipality H. This is consistent with both an amalgamation and an acquisition. Municipality G also notes that it obtains access to economic benefits or service potential that are similar to those that could have been obtained by mutual agreement; this may suggest that the economic substance of the combination is that of an acquisition, but is not conclusive.~~

Agenda item 7.1 reference: Illustrative examples (paras 39–41)
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- IE30. In considering the indicators relating to consideration, Municipality G notes that the ~~PBE public-sector~~ combination does not include the payment of consideration ~~because there is no party with an entitlement to the net assets of Municipality H (i.e., there are no former owners of Municipality H with quantifiable ownership interests)~~. This suggests that the economic substance of the combination is that of an amalgamation.
- IE31. In considering the indicators relating to the decision-making process, Municipality G notes that the ~~public-sector~~entity combination was imposed by Central Government (a third party) and that Municipality G and Municipality H had no role in determining the terms of the combination. This may suggest that the economic substance of the combination is that of an amalgamation.
- IE32. ~~Taking these factors together, On balance these factors suggest Municipality G considers that the public sector~~PBE ~~–combination should be classified as an amalgamation. In coming to this decision, Municipality G considers the absence of consideration because there is no party with an entitlement to the net assets of an operation to be the most significant factor in determining the economic substance of the combination.~~

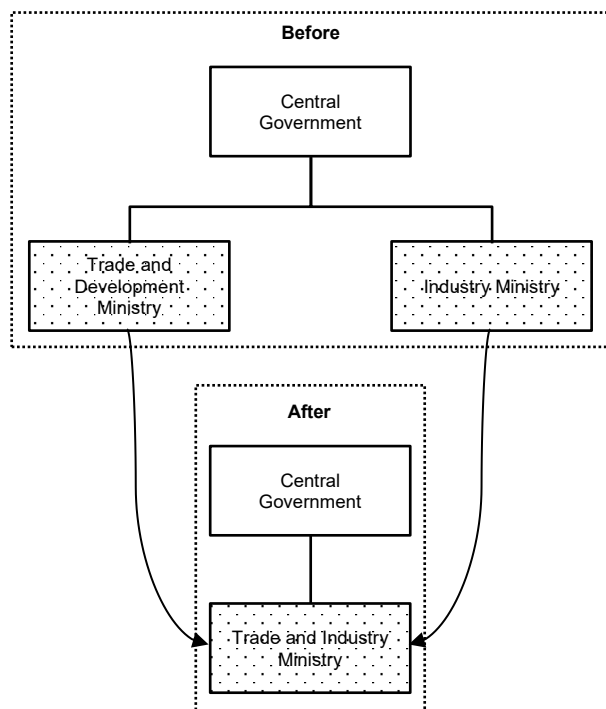
Agenda item 7.1 reference: Indicator in paragraph 12(c) (paras 10–17)
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### Scenario 3: Variation

- IE33. In scenario 3, the legislation provides for the governing body of Municipality G to become the governing body of the combined entity. In this variation, the legislation provides for a new governing body to be formed that has no links to Municipality G or Municipality H.
- IE34. In determining whether this ~~PBE public-sector~~ combination should be classified as an amalgamation or an acquisition, the first question to consider is whether one of the parties to the combination has gained control of operations as a result of the combination.
- IE35. Despite its legal form continuing, Municipality G has a newly formed governing body, unrelated to its previous governing body or that of Municipality H. Consequently, the previous Municipality G does not gain power over Municipality H. Neither does it have exposure, or rights, to variable benefits from any involvement with Municipality H.
- IE36. Municipality G has not gained control over Municipality H as a result of the ~~PBE public-sector~~ combination. Consequently the combination is classified as an amalgamation.

*Scenario 4: Restructuring of Central Government Ministries*

- IE37. The following diagram illustrates the reorganisation of Central Government ministries by combining the Trade and Development Ministry and the Industry Ministry into the newly formed Trade and Industry Ministry.



- IE38. In this scenario, a ~~PBE public sector~~ combination occurs in which the Trade and Industry Ministry is formed to combine the operations (and the related assets, liabilities and components of net assets/equity) of the Trade and Development Ministry and the Industry Ministry. All the ministries, both prior to and after the combination, are controlled by Central Government. The combination is imposed by Central Government using this control. The Trade and Development Ministry and the Industry Ministry have no role in determining the terms of the combination.
- IE39. In effecting the combination, Central Government gives responsibility for the new Trade and Industry Ministry to the Minister of Industry and the governing body of the Industry Ministry. After the combination, the Trade and Development Ministry and the Industry Ministry cease to exist.
- IE40. As Central Government controls the same operations both before and after the ~~PBE public sector~~ combination, Central Government does not report a combination in its consolidated financial statements. The combination is reported by the Trade and Industry Ministry.
- IE41. The creation of the Trade and Industry Ministry is a ~~PBE public sector~~ combination. In determining whether this should be classified as an amalgamation or an acquisition, the first question to consider is whether one of the parties to the combination has gained control of operations as a result of the combination.
- IE42. Central Government gives responsibility for the new Trade and Industry Ministry to the Minister of Industry and the governing body of the Industry Ministry. This suggests that as part of the ~~PBE public sector~~ combination that creates the new Trade and Industry Ministry, the Industry Ministry is gaining control of the operations of the Trade and Development Ministry. However, the assessment as to whether the Industry Ministry is gaining control is based on the substance of the combination, not its form. In determining whether the combination should be classified as an amalgamation or an acquisition, the Trade and Industry Ministry considers the guidance in paragraphs 7–8 and AG10–AG18 of PBE IPSAS 40.
- IE43. In this scenario, it is assumed that the decision of Central Government to give responsibility for the new Trade and Industry Ministry to the Minister of Industry and the governing body of the Industry Ministry results in the Industry Ministry gaining:

- (a) Power over the operations of the Trade and Development Ministry;
- (b) Exposure, or rights, to variable benefits from its involvement with those operations; and
- (c) The ability to use its power over those operations to affect the nature or amount of the benefits from its involvement with those operations.

IE44. The Trade and Industry Ministry concludes that, as a result of the PBE public-sector combination, the Industry Ministry has gained control of the Trade and Development Ministry. The Trade and Industry Ministry considers the guidance in paragraphs 9–14 and AG19–AG50 of PBE IPSAS 40 in determining whether the economic substance of the combination is that of an amalgamation.

IE45. ~~[Not used] In considering the economic substance of the public-sector combination, the Trade and Industry Ministry notes that the combination does not result in a controlling entity/controlled entity relationship between the Trade and Development Ministry and the Industry Ministry. This is consistent with both an amalgamation and an acquisition. The Trade and Development Ministry also notes that the Industry Ministry obtains access to economic benefits or service potential that are similar to those that could have been obtained by mutual agreement; this may suggest that the economic substance of the combination is that of an acquisition.~~

Agenda item 7.1 reference: Illustrative examples (paras 39–41)
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IE46. In considering the indicators relating to consideration, the Trade and Industry Ministry notes that the PBE public-sector combination does not include the payment of consideration because the combination took place under common control, and Central Government, the controlling entity, did not specify any consideration in the terms of the combination. Consequently, although the absence of consideration may suggest that the economic substance of the combination is that of an amalgamation, this is not of itself conclusive and other factors also need to be taken into account.

IE47. In considering the indicators relating to the decision-making process, the Trade and Industry Ministry notes that the PBE public-sector combination takes place under common control. The combination was directed by Central Government and the Trade and Development Ministry and the Industry Ministry had no role in determining the terms of the combination. This provides evidence that the ultimate decision as to whether the combination took place, and the terms of the combination, are determined by the Central Government, the controlling entity. This provides evidence that the economic substance of the combination is that of an amalgamation.

IE48. Taking these factors together, the Trade and Industry Ministry considers that the PBE public-sector combination should be classified as an amalgamation. In coming to this decision, the fact that the PBE public-sector combination takes place under common control is considered to be the most significant factor in determining the economic substance of the combination.

#### Scenario 4: Variation

IE49. In scenario 4, Central Government gives responsibility for the new Trade and Industry Ministry to the Minister of Industry and the governing body of the Industry Ministry. In this variation, Central Government appoints a new Minister and governing body.

IE50. The creation of the Trade and Industry Ministry is a PBE public-sector combination under common control. In determining whether this should be classified as an amalgamation or an acquisition, the first question to consider is whether one of the parties to the combination has gained control of operations as a result of the combination.

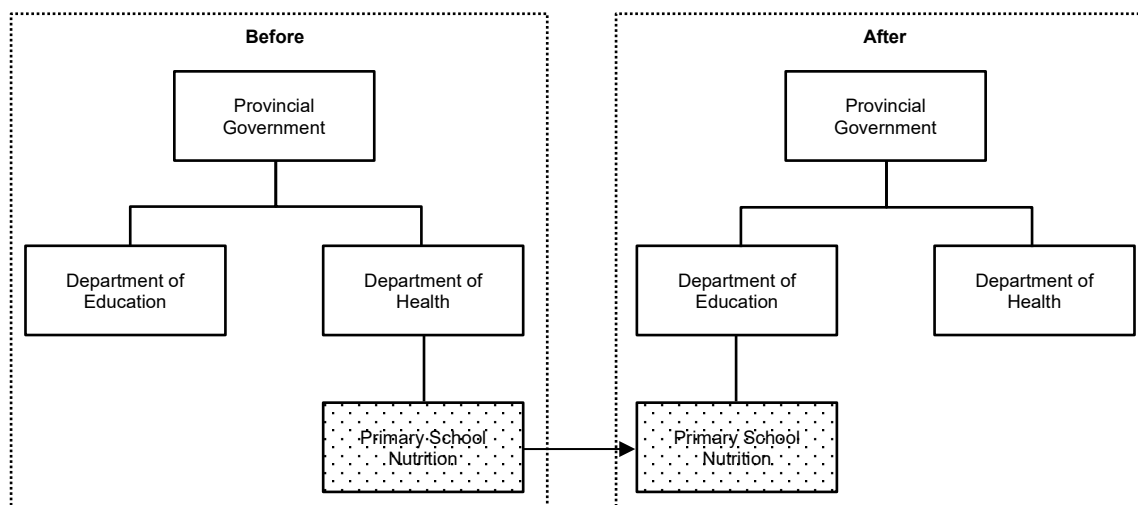
IE51. The Trade and Industry Ministry has a new Minister and a newly formed governing body, unrelated to the governing bodies of the Trade and Development Ministry and the Industry Ministry. Neither the Trade and Development Ministry or the Industry Ministry has gained power over the operations of the other ministry. Neither do they have exposure, or rights, to variable benefits from any involvement with the operations of the other ministry.

IE52. Neither of the Trade and Development Ministry nor the Industry Ministry has gained control over the Trade and Industry Ministry as a result of the PBE public-sector combination. Consequently the combination is classified as an amalgamation.



*Scenario 5: Transfer of Operations under Common Control*

IE53. The following diagram illustrates the transfer of operations between two public sector entities that are under common control.



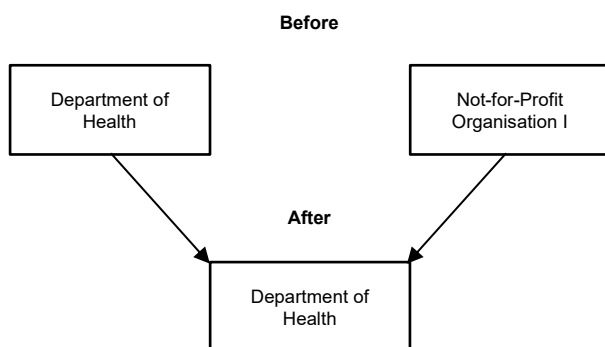
- IE54. In this scenario, a ~~PBE public sector~~ combination occurs in which the Primary School Nutrition operation is transferred from the Provincial Government's Department of Health to its Department of Education. Both departments are controlled by the Provincial Government prior to and after the combination.
- IE55. As the Provincial Government controls the same operations both before and after the ~~PBE public sector~~ combination, the Provincial Government does not report a combination in its consolidated financial statements. The combination is reported by the Department of Education.
- IE56. The transfer of the Primary School Nutrition operation is a ~~PBE public sector~~ combination. In determining whether this should be classified as an amalgamation or an acquisition, the first question the Department of Education considers is whether one of the parties to the combination has gained control of operations as a result of the combination.
- IE57. In this scenario, the Department of Education gains:
- Power over the Primary School Nutrition operation;
  - Exposure, or rights, to variable benefits from its involvement with that operation; and
  - The ability to use its power over that operation to affect the nature or amount of the benefits from its involvement with that operation.
- IE58. The Department of Education concludes that, as a result of the ~~PBE public sector~~ combination, it has gained control of the Primary School Nutrition operation. The Department of Education considers the guidance in paragraphs 9–14 and AG19–AG50 of ~~IPSAS 40~~ PBE IPSAS 40 in determining whether the economic substance of the combination is that of an amalgamation.
- IE59. ~~[Not used] In considering the economic substance of the public sector combination, the Department of Education notes that it obtains access to economic benefits or service potential that are similar to those that could have been obtained in a voluntary transaction; this may suggest that the economic substance of the combination is that of an acquisition.~~
- IE60. In considering the indicators relating to consideration, the Department of Education notes that the ~~PBE public sector~~ combination does not include the payment of consideration because the combination took place under common control, and the Provincial Government, the controlling entity, did not specify any consideration in the terms of the combination. Consequently, although the absence of consideration may suggest that the economic substance of the combination is that of an amalgamation, this is not of itself conclusive and other factors also need to be taken into account.



- IE61. In considering the indicators relating to the decision-making process, the Department of Education notes that the ~~PBE~~public sector combination takes place under common control. The combination was directed by the Provincial Government. This provides evidence that the ultimate decision as to whether the combination took place, and the terms of the combination, are determined by the Provincial Government, the controlling entity. This provides evidence that the economic substance of the combination is that of an amalgamation.
- IE62. Taking these factors together, the Department of Education considers that the ~~PBE~~public sector combination should be classified as an amalgamation. In coming to this decision, the fact that the ~~PBE~~public sector combination takes place under common control is considered to be the most significant factor in determining the economic substance of the combination.

*Scenario 6: Combination of a Public Sector Entity with a Not-For-Profit Organisation*

- IE63. The following diagram illustrates the combination of a public sector entity with a not-for-profit organisation providing similar services.



- IE64. In this scenario, a ~~PBE~~public sector combination occurs in which Not-for-Profit Organisation I, a charity which provides paramedic services, voluntarily agrees to combine with the Department of Health in order to improve the delivery of services to the public. The operations of Not-for-Profit Organisation I are integrated with similar operations provided by the Department of Health. Prior to the combination, the Department of Health has provided funding for Not-for-Profit Organisation I. The Department of Health meets the cost of transferring the title to the assets and liabilities of Not-for-Profit Organisation I incurred by the trustees of the charity.
- IE65. The combination of the Department of Health and Not-for-Profit Organisation I is a ~~PBE~~public sector combination. In determining whether this should be classified as an amalgamation or an acquisition, the first question the Department of Health considers is whether it has gained control of operations as a result of the combination.
- IE66. In this scenario, the Department of Health gains:
- Power over Not-for-Profit Organisation I and its operations;
  - Exposure, or rights, to variable benefits from its involvement with those operations; and
  - The ability to use its power over those operations to affect the nature or amount of the benefits from its involvement with those operations.
- IE67. The Department of Health concludes that, as a result of the ~~PBE~~public sector combination, it has gained control of Not-for-Profit Organisation I. The Department of Health considers the guidance in paragraphs 9–14 and AG19–AG50 of ~~IPSAS 40~~PBE IPSAS 40 in determining whether the economic substance of the combination is that of an amalgamation.
- IE68. ~~[Not used] In considering the economic substance of the public sector combination, the Department of Health notes that the combination does not result in a controlling entity/controlled entity relationship between the Department and Not for Profit Organisation I. This is consistent with both an amalgamation and an acquisition.~~

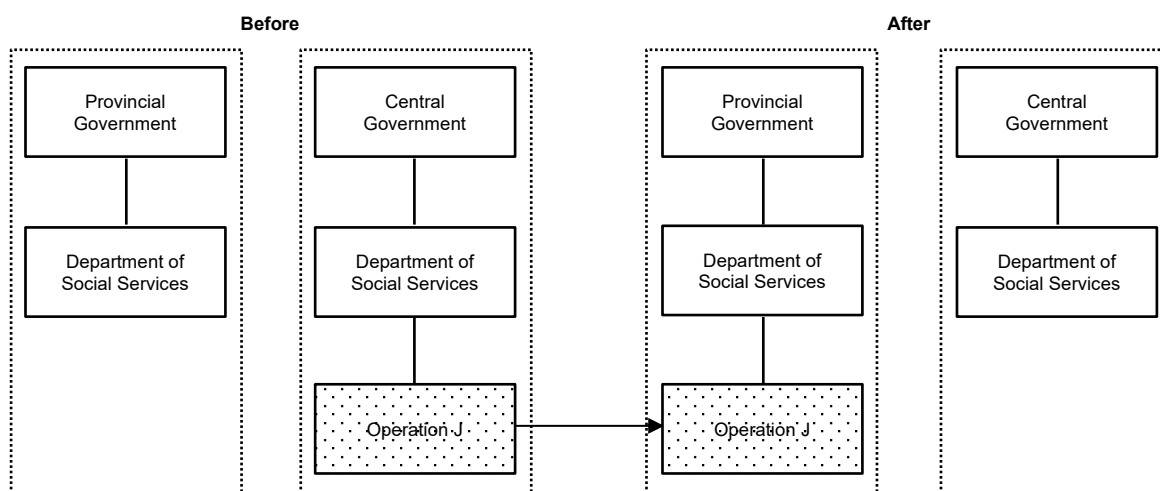
Agenda item 7.1 reference: Illustrative examples (paras 39–41)

- IE69. In considering the indicators relating to consideration, the Department of Health notes that the ~~PBE public sector~~ combination does not include the payment of consideration that is intended to compensate the seller for giving up their entitlements to the net assets of an operation. Although the Department of Health makes a payment to the trustees, this is to compensate them for costs incurred in effecting the combination, not to compensate them for giving up their entitlements to the net assets of Not-for-Profit Organisation I. ~~Although Not for Profit Organisation I has a Board of Trustees, these individuals are not entitled to the net assets of the operation. This means there is no party with an entitlement to the net assets of Not for Profit Organisation I (i.e., there are no former owners of Not for Profit Organisation I with quantifiable ownership interests). Not-for-Profit Organisation I has voluntarily surrendered the rights to their net assets to the Department of Health. This situation is similar to that of a bargain purchase. In a bargain purchase, a seller may be willing to accept a price below market value where this meets their needs, for example in enabling a quick sale. With a donated operation, the former owner is willing to transfer the operation for no consideration to their preferred counterparty. The Department of Health has obtained control of Not-for-Profit Organisation I for no consideration. In this scenario, Not-for-Profit Organisation I is willing to transfer their operation to the Department of Health because this will provide an improved delivery of services to the public. Consequently, the Department of Health concludes that the indicators of consideration do not provide any evidence to suggest that the economic substance of the combination is that of an amalgamation. This suggests that the economic substance of the combination is that of an amalgamation. In this scenario, this is confirmed by the fact that the purpose of the combination is to improve the delivery of services to the public.~~
- IE70. In considering the indicators relating to the decision-making process, the Department of Health notes that the ~~PBE public sector~~ combination was a voluntary combination. ~~Consequently, these indicators do not. This provides any evidence to suggest that the economic substance of the combination is that of an acquisition amalgamation.~~
- IE71. ~~Taking these factors together, On balance these factors suggest the Department of Health considers that the public sector PBE combination should be classified as an acquisition amalgamation. In coming to this decision, the Department of Health considers the absence of consideration because there is no party with an entitlement to the net assets of an operation to be the most significant factor in determining the economic substance of the combination. In this scenario, this view is reinforced by the fact that that Board of Trustees is voluntarily giving up control over the operations to improve the delivery of services to the public.~~

Agenda item 7.1 reference: Indicator in paragraph 12(c) (paras 10–17)

*Scenario 7: Transfer of an Operation between Levels of Government*

- IE72. The following diagram illustrates the transfer of an operation between levels of government.



- IE73. In this scenario, Central Government adopts a policy of devolving responsibility for some social services to the Provincial Government. Consequently, it proposes transferring Operation J, which provides residential care services, from Central Government's Department of Social Services to the Provincial Government's Department of Social Services. The Provincial Government supports the policy and agrees to accept Operation J. Operation J has net assets of CU1,000<sup>12</sup>. There is no transfer of consideration by the Provincial Government to the Central Government. However, the transfer agreement imposes an obligation on the Provincial Government to continue to provide the residential care services for a minimum of 10 years. Operation J does not recover all its costs from charges; the Provincial Government therefore assumes the responsibility for providing resources to meet the shortfall. Following the transfer, the Provincial Government operates Operation J as a stand-alone entity (i.e., there is a controlling entity/controlled entity relationship between the Provincial Government and Operation J), although it plans to integrate the operation with its other operations at a later date, which would remove the controlling entity/controlled entity relationship.
- IE74. The transfer of Operation J is a ~~PBE public sector~~ combination that will need to be reported in both the Provincial Government's financial statements and those of the Provincial Government's Department of Social Services. As the analysis required will be the same for both entities, this example uses the term Provincial Government to refer to both entities.
- IE75. In determining whether this should be classified as an amalgamation or an acquisition, the first question the Provincial Government considers is whether it has gained control of operations as a result of the combination.
- IE76. In this scenario, the Provincial Government gains:
- (a) Power over Operation J;
  - (b) Exposure, or rights, to variable benefits from its involvement with Operation J; and
  - (c) The ability to use its power over Operation J to affect the nature or amount of the benefits from its involvement with the operation.
- IE77. The Provincial Government concludes that, as a result of the ~~PBE public sector~~ combination, it has gained control of Operation J. The Provincial Government considers the guidance in paragraphs 9–14 and AG19–AG50 of PBE IPSAS 40 in determining whether the economic substance of the combination is that of an amalgamation.
- IE78. In considering the economic substance of the ~~PBE public sector~~ combination, the Provincial Government notes that the combination results in a controlling entity/controlled entity relationship between the Provincial Government and Operation J. This is inconsistent with the economic substance of an amalgamation.
- IE79. In considering the indicators relating to consideration, the Provincial Government notes that the ~~PBE public sector~~ combination does not include the payment of consideration that is intended to compensate the seller for giving up their entitlements to the net assets of an operation. However, the transfer agreement requires the Provincial Government to continue to provide the services. As Operation J does not recover all its costs from charges, the Provincial Government will need to provide the necessary resources to cover the shortfall. The Provincial Government considers that the cost of providing services for the agreed 10 year period is likely to be approximately equal to the value of the net assets received. It therefore considers that a market participant would estimate the fair value of Operation J (with the obligation to provide services for 10 years) to be zero. Although no consideration is transferred, this reflects the fair value of the combination. The Provincial Government concludes that the indicators relating to consideration do not provide any evidence to suggest that the economic substance of the combination is that of an amalgamation.
- IE80. In considering the indicators relating to the decision-making process, the Provincial Government notes that the ~~PBE public sector~~ combination is a voluntary combination. Consequently, these indicators do not provide any evidence to suggest that the economic substance of the combination is that of an amalgamation.

<sup>12</sup> In these examples monetary amounts are denominated in 'currency units (CU)'.

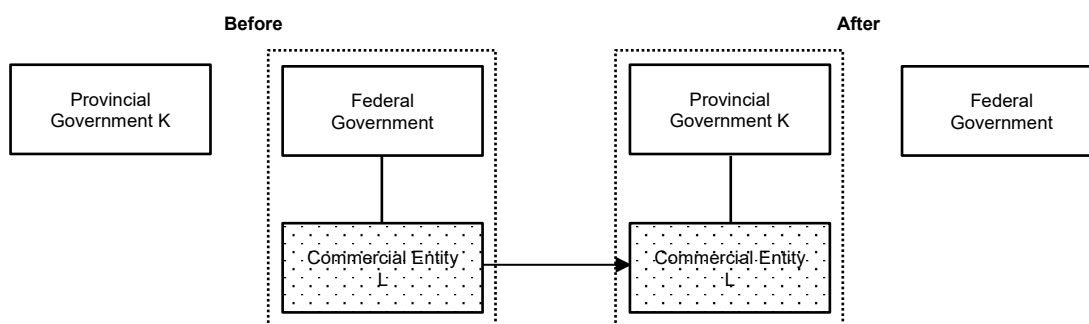
- IE81. Taking these factors together, the Provincial Government concludes that there is no evidence that economic substance of the combination is that of an amalgamation, and that the ~~PBEpublic-sector~~ combination should, therefore, be classified as an acquisition.

#### Scenario 7: Variation

- IE82. In scenario 7, the Provincial Government considers that a market participant would estimate the fair value of Operation J (with the obligation to provide services for 10 years) to be zero. This is the reason that no consideration is paid. In this variation, Operation J is assumed to cover its costs from charges. Consequently, a market participant would estimate the fair value of Operation J (with the obligation to provide services for 10 years) to be greater than zero.
- IE83. In these circumstances, the fact that the combination does not include the payment of consideration that is intended to compensate the seller for giving up their entitlements to the net assets of an operation may provide evidence that the economic substance of the combination is that of an amalgamation.
- IE84. In determining the classification of the ~~PBEpublic-sector~~ combination, the Provincial Government considers which factor or factors are the most significant. The Provincial Government considers the fact that it has gained control of Operation J and the fact that the combination does not involve the integration of its operations and those of Operation J to be the most significant factors in determining the economic substance of the combination. This suggests that the combination should be classified as an acquisition. The indicators relating to the decision-making process support this classification; only the indicators relating to consideration suggest that the economic substance of the combination may be an amalgamation. The Provincial Government therefore classifies the combination as an acquisition.

#### Scenario 8: Transfer of a Commercial Entity between Levels of Government

- IE85. The following diagram illustrates the transfer of a commercial entity between levels of government.

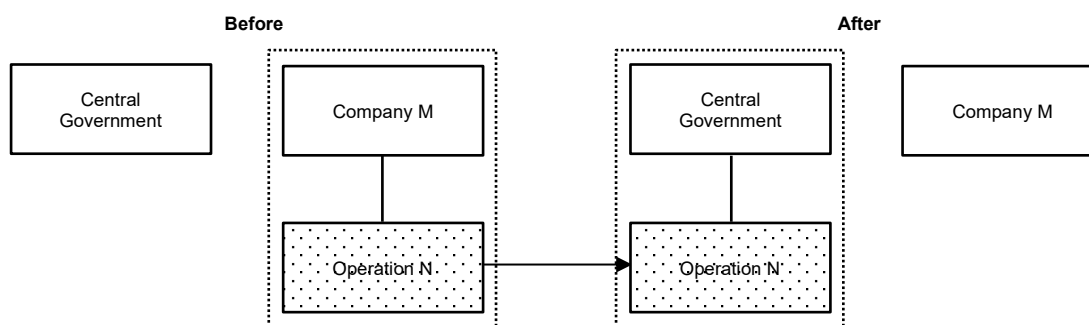


- IE86. In this scenario, the Federal Government agrees to transfer Commercial Entity L to Provincial Government K. Provincial Government K pays consideration to the Federal Government in respect of the transfer. Following the combination, Provincial Government K operates Commercial Entity L as an arms-length, stand-alone entity.
- IE87. The transfer of Commercial Entity L is a ~~PBEpublic-sector~~ combination. In determining whether this should be classified as an amalgamation or an acquisition, the first question Provincial Government K considers is whether it has gained control of operations as a result of the combination.
- IE88. In this scenario, Provincial Government K gains:
- Power over Commercial Entity L and its operations;
  - Exposure, or rights, to variable benefits from its involvement with those operations; and
  - The ability to use its power over those operations to affect the nature or amount of the benefits from its involvement with those operations.
- IE89. Provincial Government K concludes that, as a result of the ~~PBEpublic-sector~~ combination, it has gained control of Commercial Entity L. Provincial Government K considers the guidance in paragraphs 9–14 and AG19–AG50 of ~~IPSAS 40~~PBE IPSAS 40 in determining whether the economic substance of the combination is that of an amalgamation.

- IE90. In considering the economic substance of the ~~PBEpublic-sector~~ combination, Provincial Government K notes that the combination results in a controlling entity/controlled entity relationship between the Provincial Government and Commercial Entity L. This is inconsistent with the economic substance of an amalgamation. Provincial Government K also notes that the combination has commercial substance, which is suggestive of an acquisition.
- IE91. In considering the indicators relating to consideration, Provincial Government K notes that the ~~PBEpublic-sector~~ combination includes the payment of consideration that is intended to compensate the seller for giving up their entitlements to the net assets of an operation. Provincial Government K concludes that the indicators relating to consideration do not provide any evidence to suggest that the economic substance of the combination is that of an amalgamation.
- IE92. In considering the indicators relating to the decision-making process, Provincial Government K notes that the ~~PBEpublic-sector~~ combination is a voluntary combination. Consequently, these indicators do not provide any evidence to suggest that the economic substance of the combination is that of an amalgamation.
- IE93. Taking these factors together, Provincial Government K concludes that there is no evidence that the economic substance of the combination is that of an amalgamation, and that the ~~PBEpublic-sector~~ combination should, therefore, be classified as an acquisition.

*Scenario 9: Purchase of a Private Sector Operation*

- IE94. The following diagram illustrates the purchase of a private sector operation by a public sector entity.



- IE95. In this scenario, Central Government purchases Operation N from Company M. Central Government pays the market value of Operation N, and Company M acts voluntarily. Following the purchase, Operation N is managed as an arms-length, stand-alone entity.
- IE96. The purchase of Operation N is a ~~PBEpublic-sector~~ combination. In determining whether this should be classified as an amalgamation or an acquisition, the first question Central Government considers is whether it has gained control of operations as a result of the combination.
- IE97. In this scenario, Central Government gains:
- Power over Operation N;
  - Exposure, or rights, to variable benefits from its involvement with Operation N; and
  - The ability to use its power over Operation N to affect the nature or amount of the benefits from its involvement with that operation.
- IE98. Central Government concludes that, as a result of the ~~PBEpublic-sector~~ combination, it has gained control of Operation N. Central Government considers the guidance in paragraphs 9–14 and AG19–AG50 of PBE IPSAS 40 in determining whether the economic substance of the combination is that of an amalgamation.
- IE99. In considering the economic substance of the ~~PBEpublic-sector~~ combination, Central Government notes that the combination results in a controlling entity/controlled entity relationship between Central Government and Operation N. This is inconsistent with the economic substance of an amalgamation. Central Government also notes that the combination has commercial substance, which is suggestive of an acquisition.

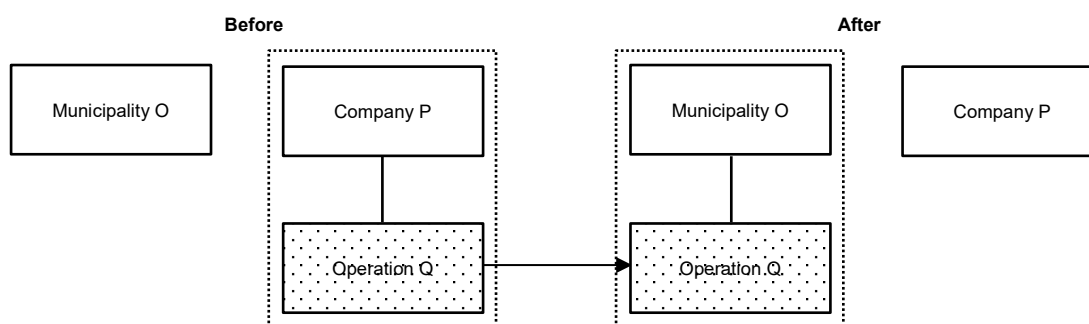
- IE100. In considering the indicators relating to consideration, Central Government notes that the PBE public sector combination includes the payment of consideration that is intended to compensate the seller for giving up their entitlements to the net assets of an operation. Central Government concludes that the indicators relating to consideration do not provide any evidence to suggest that the economic substance of the combination is that of an amalgamation.
- IE101. In considering the indicators relating to the decision-making process, Central Government notes that the PBE public sector combination is a voluntary combination. Consequently, these indicators do not provide any evidence to suggest that the economic substance of the combination is that of an amalgamation.
- IE102. Taking these factors together, Central Government concludes that there is no evidence that the economic substance of the combination is that of an amalgamation, and that the PBE public sector combination should, therefore, be classified as an acquisition.

#### Scenario 9: Variation

- IE103. In scenario 9, Company M enters into the transaction voluntarily. In this variation, Central Government nationalises Operation N through a compulsory purchase. The purchase is still effected at the market value of Operation N.
- IE104. The change from a voluntary transaction to a compulsory purchase does not affect the assessments of control or the indicators related to consideration.
- IE105. In considering the indicators relating to the decision-making process, Central Government notes that Company M does not act voluntarily. The fact that Central Government (a party to the combination) is able to impose the PBE public sector combination on Company M provides evidence that the economic substance of the combination is that of an acquisition.
- IE106. Consequently, Central Government classifies the PBE public sector combination as an acquisition.

#### Scenario 10: Bargain purchase

- IE107. The following diagram illustrates a bargain purchase by a public sector entity.



- IE108. In this scenario, Municipality O purchases Operation Q from Company P in a bargain purchase. Company P is seeking to sell Operation Q quickly to release cash for its other operations, and is willing to accept a price below the market value of Operation Q for an early sale. In entering into the bargain purchase, Company P acts voluntarily. Following the purchase, Operation Q is managed as an arms-length, stand-alone entity by Municipality O.
- IE109. The bargain purchase of Operation Q is a PBE public sector combination. In determining whether this should be classified as an amalgamation or an acquisition, the first question Municipality O considers is whether it has gained control of operations as a result of the combination.
- IE110. In this scenario, Municipality O gains:
- Power over Operation Q;
  - Exposure, or rights, to variable benefits from its involvement with Operation Q; and
  - The ability to use its power over Operation Q to affect the nature or amount of the benefits from its involvement with that operation.

- IE111. Municipality O concludes that, as a result of the ~~PBEpublic-sector~~ combination, it has gained control of Operation Q. Municipality O considers the guidance in paragraphs 9–14 and AG19–AG50 of PBE IPSAS 40 in determining whether the economic substance of the combination is that of an amalgamation.
- IE112. In considering the economic substance of the ~~PBEpublic-sector~~ combination, Municipality O notes that the combination results in a controlling entity/controlled entity relationship between Municipality O and Operation Q. This is inconsistent with the economic substance of an amalgamation. Municipality O also notes that the combination has commercial substance (even though the price paid was below the market price of Operation Q), which is suggestive of an acquisition.
- IE113. In considering the indicators relating to consideration, Municipality O notes that the ~~PBEpublic-sector~~ combination includes the payment of consideration that is intended to compensate the seller for giving up their entitlements to the net assets of an operation, even though that price was below market value. Company P voluntarily accepted a lower price for a quick sale, and the purpose of the consideration paid was to provide Company P with the level of compensation for giving up its entitlement to the net assets of Operation Q that it was willing to accept. Municipality O concludes that the indicators relating to consideration do not provide any evidence to suggest that the economic substance of the combination is that of an amalgamation.
- IE114. In considering the indicators relating to the decision-making process, Municipality O notes that the ~~PBEpublic-sector~~ combination is a voluntary combination. Consequently, these indicators do not provide any evidence to suggest that the economic substance of the combination is that of an amalgamation.
- IE115. Taking these factors together, Municipality O concludes that there is no evidence that the economic substance of the combination is that of an amalgamation, and that the ~~PBE public-sector~~ combination should, therefore, be classified as an acquisition.

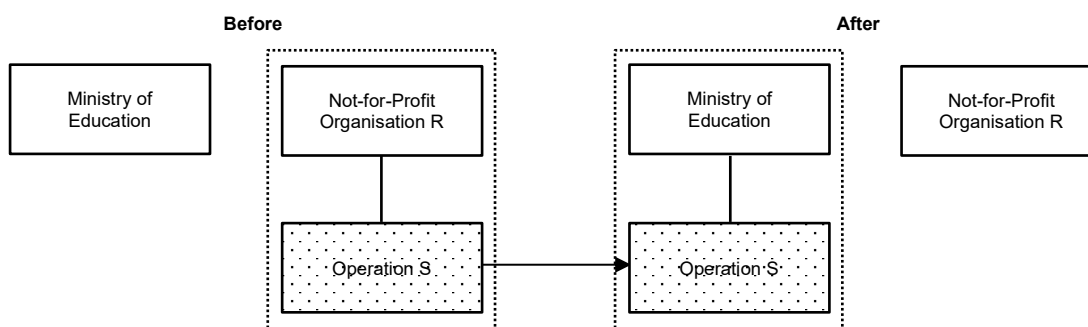
#### Scenario 10: Variation

- IE116. In scenario 10, Company P enters into the transaction voluntarily. In this variation, Municipality O seizes Operation Q through a compulsory purchase. The purchase is still effected at a price below the market value of Operation Q. Company P would not have sold Operation Q for a price below market value voluntarily.
- IE117. The change from a voluntary transaction to a compulsory purchase does not affect the assessment of control.
- IE118. In considering the indicators relating to consideration, Municipality O notes that the ~~PBEpublic-sector~~ combination includes consideration that is intended to compensate the seller for giving up their entitlements to the net assets of an operation. However, the level of compensation is less than Company P would have accepted voluntarily. Consequently, these indicators provide only weak evidence that the economic substance of the combination is that of an acquisition, and greater reliance is placed on other factors.
- IE119. In considering the indicators relating to the decision-making process, Municipality O notes that Company P does not act voluntarily. The fact that Municipality O (a party to the combination) is able to impose the ~~PBEpublic-sector~~ combination on Company P provides evidence that the economic substance of the combination is that of an acquisition.
- IE120. Taking all the factors into account, Municipality O classifies the ~~PBE public-sector~~ combination as an acquisition.



*Scenario 11: Donated Operations*

IE121. The following diagram illustrates the receipt of a donated operation by a public sector entity.

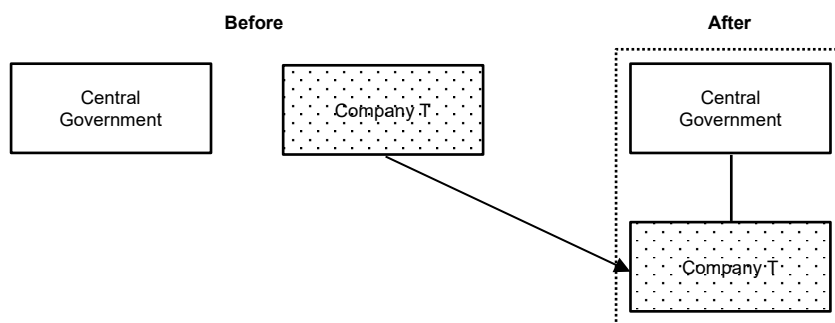


- IE122. In this scenario, Not-for-Profit Organisation R, a charity providing education services, voluntarily transfers Operation S, a school, to the Ministry of Education at no cost. Not-for-Profit Organisation R does this because it considers that this will result in improved services to the public, and enable it to meet its objectives.
- IE123. The donation of Operation S is a PBE public sector combination. In determining whether this should be classified as an amalgamation or an acquisition, the first question the Ministry of Education considers is whether it has gained control of operations as a result of the combination.
- IE124. In this scenario, the Ministry of Education gains:
- Power over Operation S;
  - Exposure, or rights, to variable benefits from its involvement with Operation S; and
  - The ability to use its power over Operation S to affect the nature or amount of the benefits from its involvement with that operation.
- IE125. The Ministry of Education concludes that, as a result of the PBE public sector combination, it has gained control of Operation S. The Ministry of Education considers the guidance in paragraphs 9–14 and AG19–AG50 of PBE IPSAS 40 in determining whether the economic substance of the combination is that of an amalgamation.
- IE126. In considering the economic substance of the PBE public sector combination, the Ministry of Education notes that the combination has commercial substance (even though no price was paid for Operation S), which is suggestive of an acquisition.
- IE127. In considering the indicators relating to consideration, the Ministry of Education notes that the PBE public sector combination does not include the payment of consideration that is intended to compensate the seller for giving up their entitlements to the net assets of an operation. However, the reason for this is that Not-for-Profit Organisation R voluntarily surrendered those rights. The situation is similar to that of a bargain purchase. In a bargain purchase, a seller may be willing to accept a price below market value where this meets their needs, for example in enabling a quick sale. With a donated operation, the former owner is willing to transfer the operation for no consideration to their preferred counterparty. In this scenario, Not-for-Profit Organisation R is willing to transfer Operation S to the Ministry of Education because this will provide improved services to the public. Consequently, the Ministry of Education concludes that the indicators of consideration do not provide any evidence to suggest that the economic substance of the combination is that of an amalgamation.
- IE128. In considering the indicators relating to the decision-making process, the Ministry of Education notes that the PBE public sector combination is a voluntary combination. Consequently, these indicators do not provide any evidence to suggest that the economic substance of the combination is that of an amalgamation.
- IE129. Taking these factors together, the Ministry of Education concludes that there is no evidence that the economic substance of the combination is that of an amalgamation, and that the PBE public sector combination should, therefore, be classified as an acquisition.



*Scenario 12: Nationalisation of a Private Sector Entity–Forced Seizure*

IE130. The following diagram illustrates the nationalisation of a private sector entity by a public sector entity by means of a forced seizure.



IE131. In this scenario, Central Government nationalizes Company T through legislation. Central Government does not pay any consideration to the shareholders of Company T. Following the purchase, Company T is managed as an arms-length, stand-alone entity.

IE132. The nationalisation of Company T is a PBE ~~public sector~~ combination. In determining whether this should be classified as an amalgamation or an acquisition, the first question Central Government considers is whether it has gained control of operations as a result of the combination.

IE133. In this scenario, Central Government gains:

- (a) Power over Company T;
- (b) Exposure, or rights, to variable benefits from its involvement with Company T; and
- (c) The ability to use its power over Company T to affect the nature or amount of the benefits from its involvement with Company T.

IE134. Central Government concludes that, as a result of the PBE ~~public sector~~ combination, it has gained control of Company T. Central Government considers the guidance in paragraphs 9–14 and AG19–AG50 of PBE IPSAS 40 in determining whether the economic substance of the combination is that of an amalgamation.

IE135. In considering the economic substance of the PBE ~~public sector~~ combination, Central Government notes that the combination results in a controlling entity/controlled entity relationship between Central Government and Company T. This is inconsistent with the economic substance of an amalgamation. Central Government also notes that, by depriving the former shareholders of their rights to Company T, the combination has commercial substance, which is suggestive of an acquisition.

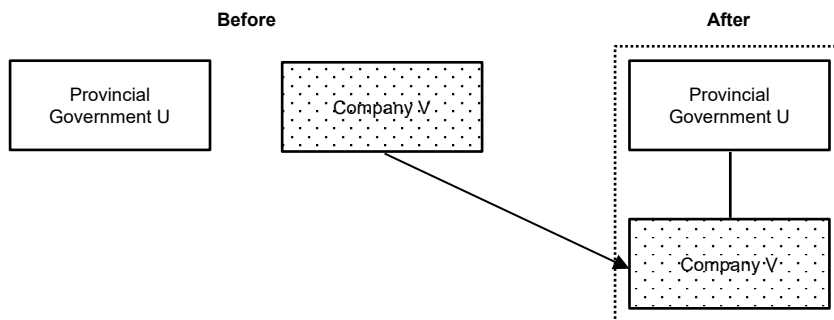
IE136. In considering the indicators relating to consideration, Central Government notes that the PBE ~~public sector~~ combination does not include the payment of consideration that is intended to compensate the seller for giving up their entitlements to the net assets of an operation. However, the former shareholders of Company T have had their entitlements extinguished through compulsion, which provides evidence that the economic substance of the combination is that of an acquisition. Central Government concludes that the indicators relating to consideration do not provide any evidence to suggest that the economic substance of the combination is that of an amalgamation.

IE137. In considering the indicators relating to the decision-making process, Central Government notes that Company T does not act voluntarily. The fact that Central Government (a party to the combination) is able to impose the ~~public sector~~ entity combination on Company T provides evidence that the economic substance of the combination is that of an acquisition.

IE138. Taking these factors together, Central Government concludes that there is no evidence that the economic substance of the combination is that of an amalgamation, and that the PBE ~~public sector~~ combination should, therefore, be classified as an acquisition.

*Scenario 13: Nationalisation of a Private Sector Entity–Bailout*

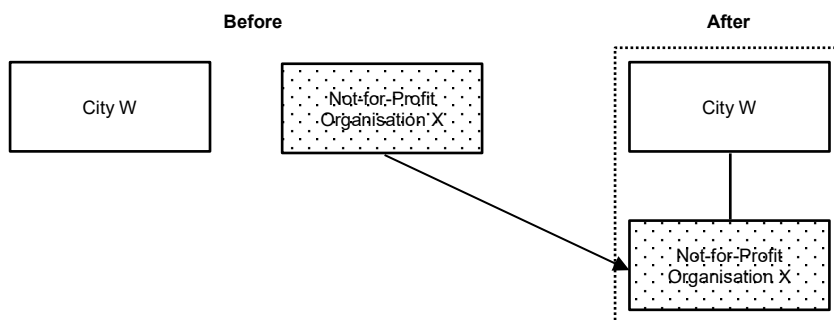
- IE139. The following diagram illustrates the nationalisation of a private sector entity by a public sector entity by means of a bailout.



- IE140. In this scenario, Provincial Government U nationalizes Company V through legislation as a result of a bailout. Prior to the nationalisation, Company V was in financial distress. Provincial Government U does not pay any consideration to the shareholders of Company V but does assume Company V's net liabilities. Following the purchase, Company V is managed as an arms-length, stand-alone entity.
- IE141. The nationalisation of Company V is a PBE public sector combination. In determining whether this should be classified as an amalgamation or an acquisition, the first question Provincial Government U considers is whether it has gained control of operations as a result of the combination.
- IE142. In this scenario, Provincial Government U gains:
- Power over Company V;
  - Exposure, or rights, to variable benefits from its involvement with Company V; and
  - The ability to use its power over Company V to affect the nature or amount of the benefits from its involvement with Company V.
- IE143. Provincial Government U concludes that, as a result of the PBE public sector combination, it has gained control of Company V. Provincial Government U considers the guidance in paragraphs 9–14 and AG19–AG50 of PBE IPSAS 40 in determining whether the economic substance of the combination is that of an amalgamation.
- IE144. In considering the economic substance of the PBE public sector combination, Provincial Government U notes that the combination results in a controlling entity/controlled entity relationship between Provincial Government U and Company V. This is inconsistent with the economic substance of an amalgamation. Provincial Government U also notes that, by assuming the net liabilities of Company V, the combination has commercial substance, which is suggestive of an acquisition.
- IE145. In considering the indicators relating to consideration, Provincial Government U notes that the PBE public sector combination does not include the payment of consideration that is intended to compensate the seller for giving up their entitlements to the net assets of an operation. However, Company V has net liabilities that are assumed by Provincial Government U as part of the combination. The lack of consideration reflects the fair value of Company V rather than suggesting that the economic substance of the combination is that of an amalgamation. Provincial Government U concludes that the indicators relating to consideration do not provide any evidence to suggest that the economic substance of the combination is that of an amalgamation.
- IE146. In considering the indicators relating to the decision-making process, Provincial Government U notes that Company V does not act voluntarily. The fact that Provincial Government U (a party to the combination) is able to impose the PBE public sector combination on Company V provides evidence that the economic substance of the combination is that of an acquisition.
- IE147. Taking these factors together, Provincial Government U concludes that there is no evidence that the economic substance of the combination is that of an amalgamation, and that the PBE public sector combination should, therefore, be classified as an acquisition.

*Scenario 14: Nationalisation of a Not-For-Profit Organisation–Bailout*

IE148. The following diagram illustrates the nationalisation of a not-for-profit organisation by a public sector entity by means of a bailout.



IE149. In this scenario, City W nationalizes Not-for-Profit Organisation X (a charity) as a result of a voluntary bailout. Prior to the nationalisation, Not-for-Profit Organisation X was in financial distress and approached City W for support. City W assumes Not-for-Profit Organisation X's net liabilities. Following the purchase, Not-for-Profit Organisation X is managed as an arms-length, stand-alone entity.

IE150. The nationalisation of Not-for-Profit Organisation X is a PBE~~public sector~~ combination. In determining whether this should be classified as an amalgamation or an acquisition, the first question City W considers is whether it has gained control of operations as a result of the combination.

IE151. In this scenario, City W gains:

- (a) Power over Not-for-Profit Organisation X;
- (b) Exposure, or rights, to variable benefits from its involvement with Not-for-Profit Organisation X; and
- (c) The ability to use its power over Not-for-Profit Organisation X to affect the nature or amount of the benefits from its involvement with Not-for-Profit Organisation X.

IE152. City W concludes that, as a result of the PBE~~public sector~~ combination, it has gained control of Not-for-Profit Organisation X. City W considers the guidance in paragraphs 9–14 and AG19–AG50 of PBE IPSAS 40 in determining whether the economic substance of the combination is that of an amalgamation.

IE153. In considering the economic substance of the PBE~~public sector~~ combination, City W notes that the combination results in a controlling entity/controlled entity relationship between City W and Not-for-Profit Organisation X. This is inconsistent with the economic substance of an amalgamation. City W also notes that, by assuming the net liabilities of Not-for-Profit Organisation X, the combination has commercial substance, which is suggestive of an acquisition.

IE154. In considering the indicators relating to consideration, City W notes that the PBE~~public sector~~ combination does not include the payment of consideration that is intended to compensate the seller for giving up their entitlements to the net assets of an operation. ~~This is because there is no party with an entitlement to the net assets of Not for Profit Organisation X (i.e., there is no former owner) as the trustees have no entitlement to the net assets.~~ This would usually provide evidence that the economic substance of the combination is that of an amalgamation. However, in this scenario Not-for-Profit Organisation X has net liabilities that are assumed by City W as part of the combination. By assuming the net liabilities, City W relieves the trustees of Not-for-Profit Organisation X of the responsibility for settling the liabilities, which is analogous to paying consideration. City W concludes, therefore, that the indicators relating to consideration do not provide any evidence to suggest that the economic substance of the combination is that of an amalgamation.

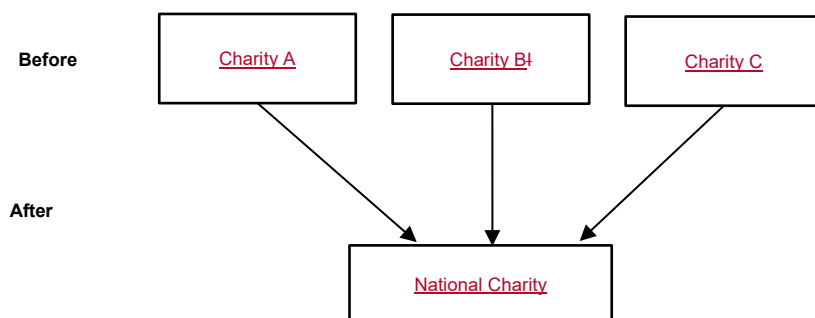
IE155. In considering the indicators relating to the decision-making process, City W notes that Not-for-Profit Organisation X voluntarily initiated the combination. City W concludes that the indicators relating to decision-making do not provide any evidence to suggest that the economic substance of the combination is that of an amalgamation.

- IE156. ~~Taking these factors together, On balance these factors suggest City W concludes that there is no evidence that the economic substance of the combination is that of an amalgamation, and that the public sector PBE-combination should, therefore, be classified as an acquisition.~~

Agenda item 7.1 reference: Indicator in paragraph 12(c) (paras 10–17)

*Scenario 15: Combination of three Charities*

- IE156.1 The following diagram illustrates the combination of three charities providing similar services in different parts of the country.



- IE156.2 In this scenario, a PBE combination occurs in which Charity A covers the South Island, Charity B covers the lower North Island and Charity C covers the upper North Island. To gain operational efficiencies and make it easier to obtain grants, donations and other funding, the three charities decide to unite their resources and activities by forming a new national registered charity, National Charity.
- IE156.3 The governing body of the National Charity is formed through the appointment of trustees from the governing bodies of charities A, B and C.
- IE156.4 All of the resources and activities of charities A, B and C are transferred to National Charity for nil consideration, whereupon charities A, B and C are wound up
- IE156.5 In determining whether the combination of charities A, B and C should be classified as an amalgamation or an acquisition, the first question to consider is whether one of the parties has gained control of operations as a result of the combination. None of the existing charities (A, B and C) gained control of the other charities. The existing charities do not have power over each other. Neither do they have exposure, or rights, to variable benefits from any involvement with National Charity.
- IE156.6 In considering the indicators relating to consideration, National Charity notes that the PBE combination does not include the payment of consideration to those with an entitlement to the net assets of charities A, B and C. This suggests that the economic substance of the combination is that of an amalgamation.
- IE156.7 In considering the indicators relating to the decision-making process, National Charity notes that none of the indicators identified in paragraph 13 are present.
- IE156.8 Charities A, B and C have not gained control of National Charity as a result of the combination. Consequently, the combination is classified as an amalgamation.

Agenda item 7.1 reference: Voluntary combination not under common control (paras 18–21)

## Accounting for Amalgamations

### Eliminating Transactions between the Combining Operations – Loans

#### *Illustrating the Consequences of Applying Paragraphs 22 and AG51–AG52 of PBE IPSAS 40*

- IE157. The following example illustrates the process for eliminating a loan between two combining operations not under common control.
- IE158. On 30 June 20X5 Resulting Entity (RE) is formed by an amalgamation of two municipalities, Combining Operation A (COA) and Combining Operation B (COB). Four years previously, COA had

provided COB with a ten year, fixed interest rate loan of CU250. Interest on the loan is payable annually, with the principal repayable on maturity.

- IE159. COB has recently experienced financial difficulties, and at the amalgamation date was in arrears on making the interest payments. The carrying amount of the financial liability (the amortized cost of the loan) in its financial statements at the amalgamation date is CU260.
- IE160. Because of the arrears and the fact that COB was experiencing financial difficulties, COA had impaired the loan. The carrying amount of the financial asset (the loan) in its financial statements at the amalgamation date is CU200.
- IE161. At the amalgamation date, RE eliminates the financial asset received from COA and the financial liability assumed from COB and credits components of net assets/equity with CU60, the difference between the carrying amounts of the financial asset and the financial liability associated with the loan.

### **Eliminating Transactions between the Combining Operations – Transfers**

*Illustrating the Consequences of Applying Paragraphs 22 and AG51–AG52 of PBE IPSAS 40*

- IE162. The following example illustrates the process for eliminating a transfer between two combining operations not under common control.
- IE163. On 30 June 20X9, Resulting Entity (RE) is formed by an amalgamation of two government agencies, Combining Operation A (COA) and Combining Operation B (COB). On 1 January 20X9, COA had provided COB with a grant of CU700 to be used in the provision of an agreed number of training courses.
- IE164. The grant was subject to a condition that the grant would be returned proportionately to the number of training courses not delivered. At the amalgamation date, COB had delivered half of the agreed number of courses, and recognised a liability of CU350 in respect of its performance obligation, in accordance with PBE IPSAS 23 *Revenue from Non-Exchange Transactions* ~~(*Taxes and Transfers*)~~. Based on past experience, COA considered that COB was more likely than not to deliver the training courses. It was therefore not probable that there would be a flow of resources to COA, and COA did not recognise an asset in respect of the grant, but accounted for the full CU700 as an expense.
- IE165. At the amalgamation date, the transaction is eliminated. There is no longer an obligation to an external party. The resulting entity does not recognise a liability for the CU350, but instead recognises this amount in net assets/equity.

### **Adjusting the Carrying Amounts of the Identifiable Assets and Liabilities of the Combining Operations to Conform to the Resulting Entity's Accounting Policies in an Amalgamation**

*Illustrating the Consequences of Applying Paragraphs 26–27 and 36 of PBE IPSAS 40*

- IE166. The following example illustrates the process for adjusting the carrying amounts of the identifiable assets and liabilities of the combining operations to conform to the resulting entity's accounting policies in an amalgamation under common control.
- IE167. On 1 October 20X5 RE is formed by an amalgamation of two government departments, COA and COB. COA has previously adopted an accounting policy of measuring property, plant and equipment using the cost model in PBE IPSAS 17 *Property, Plant and Equipment*. COB has previously adopted an accounting policy of measuring property, plant and equipment using the revaluation model in PBE IPSAS 17.
- IE168. RE adopts an accounting policy of measuring property, plant and equipment using the revaluation model. RE seeks an independent valuation for the items of property, plant and equipment previously controlled by COA.
- IE169. On receiving the independent valuation for the items of property, plant and equipment previously controlled by COA, RE adjusts the carrying amounts of the items of property, plant and equipment as follows, with the corresponding entry being made to components of net assets/equity:

Class of Asset	Carrying Amount (CU)	Valuation (CU)	Adjustment (CU)
Land	17,623	18,410	787
Buildings	35,662	37,140	1,478
Vehicles	1,723	1,605	(118)

- IE170. RE also reviews the carrying amounts of the items of property, plant and equipment previously controlled by COB to ensure the amounts are up to date as at 1 October 20X5. The review confirms the carrying amounts of the items of property, plant and equipment previously controlled by COB are up to date and that no adjustment is required.
- IE171. RE recognises the items of property, plant and equipment previously controlled by COB at their carrying amounts. In accordance with paragraph 67 of PBE IPSAS 17, RE will review the residual values and useful lives of the plant and equipment previously controlled by both COA and COB at least at each annual reporting date. If expectations differ from previous estimates, RE will account for these changes as changes in accounting estimates, in accordance with PBE IPSAS 3, *Accounting Policies, Changes in Accounting Estimates and Errors*.

### Forgiveness of amounts of tax due in an amalgamation

*Illustrating the Consequences of Accounting for Tax Forgiveness in an Amalgamation by Applying Paragraphs 33–34 and AG57–AG58 of PBE IPSAS 40*

- IE172. The following example illustrates the accounting for an amalgamation not under common control in which the resulting entity's tax liability is forgiven as part of the terms of the amalgamation.
- IE173. On 1 January 20X6 RE is formed by an amalgamation of two public sector entities, COA and COB. The amalgamation is directed by the national government. RE, COA and COB have the same accounting policies; no adjustment to the carrying amounts of the identifiable assets and liabilities of the COA and COB to conform to the resulting entity's accounting policies is required. At the date of the amalgamation, there are no amounts outstanding between COA and COB.
- IE174. In its statement of financial position as at 1 January 20X6, RE recognises and measures the assets and liabilities of COA and COB at their carrying amounts in their respective financial statements as of the amalgamation date:

Statement of Financial Position:	COA (CU)	COB (CU)	RE (CU)
Financial assets	1,205	997	2,202
Inventory	25	42	67
Property, plant and equipment	21,944	18,061	40,005
Identifiable intangible assets	0	3,041	3,041
Financial liabilities	(22,916)	(22,020)	(44,936)
Tax liabilities	(76)	(119)	(195)
Total net assets	182	2	184
Net Assets/Equity	182	2	184

- IE175. Suppose that the terms of the amalgamation include the Ministry of Finance (MF) (the tax authority) forgiving RE's tax liability. RE would derecognise the tax liability and make the adjustment to net assets/equity. The statement of financial position as at 1 January 20X6 for RE would be as follows:

<b>Statement of Financial Position:</b>	<b>RE (CU)</b>
Financial assets	2,202
Inventory	67
Property, plant and equipment	40,005
Intangible assets	3,041
Financial liabilities	(44,936)
Tax liabilities	0
Total net assets	379
Net Assets/Equity	379

- IE176. MF **would recognise an adjustment for the tax forgiven, and** accounts for **the remaining** tax receivable in accordance with PBE IPSAS 23, ~~and would recognise an adjustment for the tax forgiven.~~

Agenda item 7.1 reference: Tax forgiven (paras 22–27)

### **Recognising and Measuring Components of Net Assets/Equity Arising as a Result of an Amalgamation**

#### *Illustrating the Consequences of Applying Paragraphs 37–39 of PBE IPSAS 40*

- IE177. The following example illustrates the accounting for recognising and measuring components of net assets/equity in an amalgamation.
- IE178. On 1 June 20X4, a new municipality RE is formed by the amalgamation of operations COA and COB relating to two geographical areas of other municipalities, not previously under common control.
- IE179. COB has previously performed services for COA for which it was to be paid CU750. Payment was outstanding at the amalgamation date. This transaction formed part of the carrying amount of financial liabilities for COA and part of the carrying amount of financial assets for COB.
- IE180. COA has previously adopted an accounting policy of measuring property, plant and equipment using the cost model. COB has previously adopted an accounting policy of measuring property, plant and equipment using the revaluation model. RE has adopted an accounting policy of measuring property, plant and equipment using the revaluation model. RE obtains an independent valuation for the items of property, plant and equipment previously controlled by COA. As a result, it increases its carrying amount for those items of the property, plant and equipment by CU5,750 and makes the corresponding adjustment to components of net assets/equity.



- IE181. The carrying amounts of the assets, liabilities and components of net assets/equity transferred are summarised below. Adjustments to eliminate transactions between COA and COB (see paragraph 22), and to conform the carrying amounts to the resulting entity's accounting policies are also shown.

	COA (CU)	COB (CU)	Elimination Adjustments (CU)	Accounting Policy Adjustments (CU)	RE Opening Balance (CU)
Financial Assets	11,248	17,311	(750)		27,809
Inventory	1,072	532			1,604
Property, plant and equipment	5,663	12,171		5,750	23,584
Intangible assets	0	137			137
Financial liabilities	(18,798)	(20,553)	750		(38,601)
Total net assets/(liabilities)	(815)	9,598		5,750	14,533
Revaluation surplus	0	6,939		5,750	12,689
<del>Accumulated surpluses or deficits</del> <u>Accumulate d comprehensive revenue and expense</u>	(815)	2,659			1,844
Total net assets/equity	(815)	9,598	0	5,750	14,533

- IE182. In accordance with paragraphs 37–39 of PBE IPSAS 40, RE may present net assets/equity as either a single opening balance of CU14,533 or as the separate components shown above.
- IE183. The other municipalities that, prior to the amalgamation, controlled COA and COB would derecognise the assets, liabilities and components of net assets/equity transferred to RE in accordance with other PBE Standards.

### Measurement Period in an Amalgamation

#### *Illustrating the Consequences of Applying Paragraphs 40–44 of PBE IPSAS 40.*

- IE184. If the initial accounting for an amalgamation is not complete at the end of the financial reporting period in which the amalgamation occurs, paragraph 40 of PBE IPSAS 40 requires the resulting entity to recognise in its financial statements provisional amounts for the items for which the accounting is incomplete. During the measurement period, the resulting entity recognises adjustments to the provisional amounts needed to reflect new information obtained about facts and circumstances that existed as of the amalgamation date and, if known, would have affected the measurement of the amounts recognised as of that date. Paragraph 43 of PBE IPSAS 40 requires the resulting entity to recognise such adjustments as if the accounting for the amalgamation had been completed at the amalgamation date. Measurement period adjustments are not included in surplus or deficit.
- IE185. Suppose that RE is formed by the amalgamation of COA and COB (two municipalities that were not under common control prior to the amalgamation) on 30 November 20X3. Prior to the amalgamation,



COA had an accounting policy of using the revaluation model for measuring land and buildings, whereas COB's accounting policy was to measure land and buildings using the cost model. RE adopts an accounting policy of measuring land and buildings using the revaluation model, and seeks an independent valuation for the land and buildings previously controlled by COB. This valuation was not complete by the time RE authorised for issue its financial statements for the year ended 31 December 20X3. In its 20X3 annual financial statements, RE recognised provisional values for the land and buildings of CU150,000 and CU275,000 respectively. At the amalgamation date, the buildings had a remaining useful life of fifteen years. The land had an indefinite life. Four months after the amalgamation date, RE received the independent valuation, which estimated the amalgamation-date value of the land as CU160,000 and the amalgamation-date value of the buildings as CU365,000.

- IE186. In its financial statements for the year ended 31 December 20X4, RE retrospectively adjusts the 20X3 prior year information as follows:
- (a) The carrying amount of the land as of 31 December 20X3 is increased by CU10,000. As the land has an indefinite life, no depreciation is charged.
  - (b) The carrying amount of the buildings as of 31 December 20X3 is increased by CU89,500. That adjustment is measured as the valuation adjustment at the amalgamation date of CU90,000 less the additional depreciation that would have been recognised if the asset's value at the amalgamation date had been recognised from that date (CU500 for one month's depreciation).
  - (c) An adjustment of CU100,000 is recognised in net assets/equity as of 31 December 20X3.
  - (d) Depreciation expense for 20X3 is increased by CU500.
- IE187. In accordance with paragraph 56 of PBE IPSAS 40, RE discloses:
- (a) In its 20X3 financial statements, that the initial accounting for the amalgamation has not been completed because the valuation of land and buildings previously controlled by COB has not yet been received.
  - (b) In its 20X4 financial statements, the amounts and explanations of the adjustments to the provisional values recognised during the current reporting period. Therefore, RE discloses that the 20X3 comparative information is adjusted retrospectively to increase the value of the land and buildings by CU99,500 (CU100,000 at the amalgamation date), an increase in depreciation expense of CU500 and an increase in net assets/equity of CU100,000.

### **Subsequent Measurement of a Transfer Received by a Combining Operation on the Basis of Criteria that may Change as a Result of an Amalgamation**

*Illustrating the Consequences of Applying the Requirements in Paragraphs 48 and AG61–AG63 of PBE IPSAS 40.*

- IE188. The following example illustrates the subsequent accounting for a transfer received by a combining operation on the basis of criteria that may change as a result of an amalgamation.
- IE189. On 1 January 20X3, a national government provides an annual grant to those municipalities where the average household income is below a threshold. On 1 June 20X3, RE, a new municipality, is formed by the amalgamation of two existing municipalities, COA and COB. COA had previously received a grant of CU1,000, based on its average household income. COB has received no grant as its average household income was above the threshold.
- IE190. Following the amalgamation on 1 June 20X3, the average household income of RE is above the threshold that the government had set when allocating grants.
- IE191. On 1 July 20X3, the national government requires RE to repay a portion (CU200) of the grant previously paid to COA. RE recognises a liability and an expense of CU200 on 1 July 20X3.

### **Disclosure Requirements Relating to Amalgamations**

*Illustrating the Consequences of Applying the Disclosure Requirements in Paragraphs 53–57 of PBE IPSAS 40.*

- IE192. The following example illustrates some of the disclosure requirements relating to amalgamations of PBE IPSAS 40; it is not based on an actual transaction. The example assumes that RE is a newly created municipality formed by amalgamating the former municipalities COA and COB. The illustration presents

the disclosures in a tabular format that refers to the specific disclosure requirements illustrated. An actual footnote might present many of the disclosures illustrated in a simple narrative format.

**Paragraph  
reference**

54(a)–(c) On 30 June 20X2 RE was formed by an amalgamation of the former municipalities COA and COB. Neither COA nor COB gained control of RE in the amalgamation. The amalgamation was mutually agreed by COA and COB, and enacted by the Government through legislation. The amalgamation aims to reduce costs through economies of scale, and to provide improved services to residents.

54(d) **Amounts recognised for each major class of assets and liabilities transferred as at 30 June 20X2**

	CU
Financial assets	1,701
Inventory	5
Property, plant and equipment	74,656
Intangible assets	42
Financial liabilities	(2,001)
Total net assets	<u>74,403</u>

54(e) The following adjustments have been made to the carrying amounts of assets and liabilities recorded by COA and COB as at 30 June 20X2 prior to the amalgamation:

		<b>Original Amount (CU)</b>	<b>Adjustment (CU)</b>	<b>Revised Amount (CU)</b>
54(e)(i)	Restatement of financial assets recorded by COA to eliminate transactions with COB	822	(25)	797
54(e)(i)	Restatement of financial liabilities recorded by COB to eliminate transactions with COA	(1,093)	25	(1,068)
54(e)(ii)	Restatement of property plant and equipment recorded by COA to measure the items using the revaluation model	12,116	17,954	30,070

**Paragraph  
reference**

54(f)

**Amounts recognised in Net Assets/Equity as at 30 June 20X2**

	<b>COA (CU)</b>	<b>COB (CU)</b>	<b>Adjustment (CU)</b>	<b>RE (CU)</b>
Revaluation surplus	0	18,332	17,954	36,286
<del>Accumulated surpluses or deficits</del> <u>Accumulated comprehensive revenue and expense</u>	12,047	26,070	0	38,117
Total net assets/equity	12,047	44,402	17,954	74,403

54(h)

At the time these financial statements were authorised for issue, the last reporting date for COA and COB was 31 December 20X1. The revenue and expense, and surplus or deficit for COA and COB from 1 January 20X2 to the amalgamation date (30 June 20X2), and the amounts reported by COA and COB for each major class of assets and liabilities, and for components of net assets/equity, is shown below:

	<b>COA (CU)</b>	<b>COB (CU)</b>
<b>54(h)(i) Revenue</b>		
Property taxes	45,213	70,369
Revenue from exchange transactions	2,681	25,377
Transfers from other government entities	32,615	19,345
<b>Total revenue</b>	<b>80,509</b>	<b>115,091</b>
<b>54(h)(i) Expenses</b>		
Wages, salaries and employee benefits	(51,263)	(68,549)
Grants and other transfer payments	(18,611)	(26,445)
Supplies and consumables used	(7,545)	(13,391)
Depreciation expense	(677)	(2,598)
Impairment of property, plant and equipment	(17)	(33)
Finance costs	(2)	(3)
<b>Total expenses</b>	<b>(78,115)</b>	<b>(111,019)</b>
<b>54(h)(i) Surplus or (deficit) for the period 1 January 20X2 to 30 June 20X2</b>	<b>2,394</b>	<b>4,072</b>

54(h)(ii)	<b>Assets as at 30 June 20X2</b>		
	Financial assets	822	904
	Inventory	0	5
	Property, plant and equipment	12,116	44,586
	Intangible assets	42	0
	<b>Total Assets</b>	<b>12,980</b>	<b>45,495</b>
54(h)(ii)	<b>Liabilities as at 30 June 20X2</b>		
	Financial liabilities	(933)	(1,093)
	<b>Total liabilities</b>	<b>(933)</b>	<b>(1,093)</b>
54(h)(iii)	<b>Net assets as at 30 June 20X2</b>	<b>12,047</b>	<b>44,402</b>
	<b>Net assets/equity as at 30 June 20X2</b>		
	Revaluation surplus	0	18,332
	<del>Accumulated surpluses or deficits</del> <u>Accumulated comprehensive revenue and expense</u>	12,047	26,070
	<b>Total net assets/equity as at 30 June 20X2</b>	<b>12,047</b>	<b>44,402</b>

In considering the disclosures related to an amalgamation, an entity may find it helpful to refer to the discussion of materiality in PBE IPSAS 1 *Presentation of Financial Statements*.

## Accounting for Acquisitions

### Reverse Acquisitions

*Illustrating the Consequences of Recognising a Reverse Acquisition by Applying Paragraphs AG66–AG71 of PBE IPSAS 40*

- IE193. This example illustrates the accounting for a reverse acquisition in which Entity B, the legal controlled entity, acquires Entity A, the entity issuing equity instruments and therefore the legal controlling entity, in a reverse acquisition on 30 September 20X6. This example ignores the accounting for any income tax effects.
- IE194. The statements of financial position of Entity A and Entity B immediately before the acquisition are:

	<b>Entity A</b> <b>(legal controlling</b> <b>entity, accounting</b> <b>acquired operation)</b> <b>CU</b>	<b>Entity B</b> <b>(legal controlled</b> <b>entity, accounting</b> <b>acquirer)</b> <b>CU</b>
Current assets	500	700
Non-current assets	1,300	3,000
Total assets	<u>1,800</u>	<u>3,700</u>

	Entity A (legal controlling entity, accounting acquired operation) CU	Entity B (legal controlled entity, accounting acquirer) CU
Current liabilities	300	600
Non-current liabilities	400	1,100
Total liabilities	700	1,700
Shareholders' equity		
<del>Accumulated surplus</del> <u>Accumulated comprehensive revenue and expense or deficit</u>	800	1,400
Issued equity		
100 ordinary shares	300	
60 ordinary shares		600
Total shareholders' equity	1,100	2,000
Total liabilities and shareholders' equity	1,800	3,700

IE195. This example also uses the following information:

- On 30 September 20X6 Entity A issues 2.5 shares in exchange for each ordinary share of Entity B. Entity B's sole shareholder, a government, exchanges its shares in Entity B. Therefore, Entity A issues 150 ordinary shares in exchange for all 60 ordinary shares of Entity B.
- The fair value of each ordinary share of Entity B at 30 September 20X6 is CU40. The quoted market price of Entity A's ordinary shares at that date is CU16.
- The fair values of Entity A's identifiable assets and liabilities at 30 September 20X6 are the same as their carrying amounts, except that the fair value of Entity A's non-current assets at 30 September 20X6 is CU1,500.

*Calculating the Fair Value of the Consideration Transferred*

IE196. As a result of Entity A (legal controlling entity, accounting acquired operation) issuing 150 ordinary shares, Entity B's shareholder (the government) owns 60 percent of the issued shares of the combined entity (i.e., 150 of 250 issued shares). The remaining 40 percent are owned by Entity A's shareholders. If the acquisition had taken the form of Entity B issuing additional ordinary shares to Entity A's shareholders in exchange for their ordinary shares in Entity A, Entity B would have had to issue 40 shares for the ratio of ownership interest in the combined entity to be the same. Entity B's shareholder (the government) would then own 60 of the 100 issued shares of Entity B—60 percent of the combined entity. As a result, the fair value of the consideration effectively transferred by Entity B and the group's interest in Entity A is CU1,600 (40 shares with a fair value per share of CU40).

IE197. The fair value of the consideration effectively transferred should be based on the most reliable measure. In this example, the quoted price of Entity A's shares in the principal (or most advantageous) market for the shares provides a more reliable basis for measuring the consideration effectively transferred

than the fair value of the shares in Entity B, and the consideration is measured using the market price of Entity A's shares—100 shares with a fair value per share of CU16.

### *Measuring Goodwill*

- IE198. Goodwill is measured as the excess of the fair value of the consideration effectively transferred (the group's interest in Entity A) over the net amount of Entity A's recognised identifiable assets and liabilities, as follows:

	CU	CU
Consideration effectively transferred		1,600
Net recognised values of Entity A's identifiable assets and liabilities		
Current assets	500	
Non-current assets	1,500	
Current liabilities	(300)	
Non-current liabilities	<u>(400)</u>	<u>(1,300)</u>
Goodwill		<u>300</u>

### *Consolidated statement of financial position at 30 September 20X6*

- IE199. The consolidated statement of financial position immediately after the acquisition is:

	CU
Current assets [CU700 + CU500]	1,200
Non-current assets [CU3,000 + CU1,500]	4,500
Goodwill	<u>300</u>
Total assets	<u>6,000</u>
Current liabilities [CU600 + CU300]	900
Non-current liabilities [CU1,100 + CU400]	<u>1,500</u>
Total liabilities	<u>2,400</u>
Shareholders' equity	
<del>Accumulated surplus</del> Accumulated comprehensive revenue and expense or deficit	1,400
Issued equity	
250 ordinary shares [CU600 + CU1,600]	<u>2,200</u>
Total shareholders' equity	<u>3,600</u>
Total liabilities and shareholders' equity	<u>6,000</u>

- IE200. The amount recognised as issued equity interests in the consolidated financial statements (CU2,200) is determined by adding the issued equity of the legal controlled entity immediately before the acquisition (CU600) and the fair value of the consideration effectively transferred (CU1,600). However, the equity structure appearing in the consolidated financial statements (i.e., the number and type of equity interests issued) must reflect the equity structure of the legal controlling entity, including the equity interests issued by the legal controlling entity to effect the combination.

*Non-controlling interest*

- IE201. Assume the same facts as above, except that Entity B has more than one shareholder, and that only 56 of Entity B's 60 ordinary shares are exchanged. Because Entity A issues 2.5 shares in exchange for each ordinary share of Entity B, Entity A issues only 140 (rather than 150) shares. As a result, Entity B's shareholders own 58.3 percent of the issued shares of the combined entity (140 of 240 issued shares). The fair value of the consideration transferred for Entity A, the accounting acquired operation, is calculated by assuming that the combination had been effected by Entity B issuing additional ordinary shares to the shareholders of Entity A in exchange for their ordinary shares in Entity A. That is because Entity B is the accounting acquirer, and paragraph AG67 of PBE IPSAS 40 requires the acquirer to measure the consideration exchanged for the accounting acquired operation.
- IE202. In calculating the number of shares that Entity B would have had to issue, the non-controlling interest is excluded from the calculation. The majority shareholder (the government) owns 56 shares of Entity B. For that to represent a 58.3 percent equity interest, Entity B would have had to issue an additional 40 shares. The majority shareholder (the government) would then own 56 of the 96 issued shares of Entity B and, therefore, 58.3 percent of the combined entity. As a result, the fair value of the consideration transferred for Entity A, the accounting acquired operation, is CU1,600 (i.e., 40 shares, each with a fair value of CU40). That is the same amount as when Entity B's sole shareholder tenders all 60 of its ordinary shares for exchange. The recognised amount of the group's interest in Entity A, the accounting acquired operation, does not change if some of Entity B's shareholders do not participate in the exchange.
- IE203. The non-controlling interest is represented by the four shares of the total 60 shares of Entity B that are not exchanged for shares of Entity A. Therefore, the non-controlling interest is 6.7 percent. The non-controlling interest reflects the proportionate interest of the non-controlling shareholders in the pre-combination carrying amounts of the net assets of Entity B, the legal controlled entity. Therefore, the consolidated statement of financial position is adjusted to show a non-controlling interest of 6.7 percent of the pre-combination carrying amounts of Entity B's net assets (i.e., CU134 or 6.7 percent of CU2,000).
- IE204. The consolidated statement of financial position at 30 September 20X6, reflecting the non-controlling interest, is as follows:

	CU
Current assets [CU700 + CU500]	1,200
Non-current assets [CU3,000 + CU1,500]	4,500
Goodwill	300
Total assets	<u>6,000</u>
Current liabilities [CU600 + CU300]	900
Non-current liabilities [CU1,100 + CU400]	1,500
Total liabilities	<u>2,400</u>
Shareholders' equity	
Accumulated <del>comprehensive revenue and expense surplus or deficit</del> [CU1,400 × 93.3 percent]	1,306
Issued equity	
240 ordinary shares [CU560 + CU1,600]	2,160
Non-controlling interest	134
Total shareholders' equity	<u>3,600</u>
Total liabilities and shareholders' equity	<u>6,000</u>

- IE205. The non-controlling interest of CU134 has two components. The first component is the reclassification of the non-controlling interest's share of the accounting acquirer's retained earnings immediately before the acquisition ( $\text{CU}1,400 \times 6.7$  percent or CU93.80). The second component represents the reclassification of the non-controlling interest's share of the accounting acquirer's issued equity ( $\text{CU}600 \times 6.7$  percent or CU40.20).

### Identifiable Intangible Assets in an Acquisition

#### *Illustrating the Consequences of Applying Paragraphs 64–68 and AG75–AG84 of PBE IPSAS 40*

- IE206. The following are examples of identifiable intangible assets acquired in an acquisition. Some of the examples may have characteristics of assets other than intangible assets. The acquirer should account for those assets in accordance with their substance. The examples are not intended to be all-inclusive.
- IE207. Intangible assets identified as having a 'binding arrangement' basis are those that arise from binding arrangements (including rights from contracts or other legal rights). Those designated as having a 'no binding arrangement' basis do not arise from binding arrangements but are separable. Intangible assets identified as having a binding arrangement basis might also be separable but separability is not a necessary condition for an asset to meet the binding arrangement criterion.

#### *Marketing-Related Intangible Assets*

- IE208. Marketing-related intangible assets are used primarily in the marketing or promotion of products or services. Examples of marketing-related intangible assets are:

Class	Basis
Trademarks, trade names, service marks, collective marks and certification marks	Binding arrangement
Trade dress (unique colour, shape or package design)	Binding arrangement
Newspaper mastheads	Binding arrangement
Internet domain names	Binding arrangement
Non-competition agreements	Binding arrangement

#### Trademarks, Trade Names, Service Marks, Collective Marks and Certification Marks

- IE209. Trademarks are words, names, symbols or other devices used in trade to indicate the source of a product and to distinguish it from the products of others. A service mark identifies and distinguishes the source of a service rather than a product. Collective marks identify the goods or services of members of a group. Certification marks certify the geographical origin or other characteristics of a good or service.
- IE210. Trademarks, trade names, service marks, collective marks and certification marks may be protected legally through registration with governmental agencies, continuous use in commerce or by other means. If it is protected legally through registration or other means, a trademark or other mark acquired in an acquisition is an intangible asset that meets the binding arrangement criterion. Otherwise, a trademark or other mark acquired in an acquisition can be recognised separately from goodwill if the separability criterion is met, which normally it would be.
- IE211. The terms *brand* and *brand name*, often used as synonyms for trademarks and other marks, are general marketing terms that typically refer to a group of complementary assets such as a trademark (or service mark) and its related trade name, formulas, recipes and technological expertise. PBE IPSAS 40 does not preclude an entity from recognising, as a single asset separately from goodwill, a group of complementary intangible assets commonly referred to as a brand if the assets that make up that group have similar useful lives.



## Internet Domain Names

- IE212. An Internet domain name is a unique alphanumeric name that is used to identify a particular numeric Internet address. Registration of a domain name creates an association between that name and a designated computer on the Internet for the period of the registration. Those registrations are renewable. A registered domain name acquired in an acquisition meets the binding arrangement criterion.

*Service User or Customer-Related Intangible Assets*

- IE213. Examples of service user or customer-related intangible assets are:

<b>Class</b>	<b>Basis</b>
Lists of users of a service	No binding arrangement
Order or production backlog	Binding arrangement
Customer binding arrangements and the related customer relationships	Binding arrangement
Customer relationships arising through means other than binding arrangements	No binding arrangement

## Lists of Users of a Service

- IE214. A list of users of a service consists of information about service users, such as their names and contact information. A list of users of a service also may be in the form of a database that includes other information about the users, such as their service use histories and demographic information. A list of users of a service does not usually arise from a binding arrangement (including rights from contracts or other legal rights). However, lists of users of a service are often leased or exchanged. Therefore, a list of users of a service acquired in an acquisition normally meets the separability criterion.

## Order or Production Backlog

- IE215. An order or production backlog arises from binding arrangements such as purchase or sales orders. An order or production backlog acquired in an acquisition meets the binding arrangement criterion even if the purchase or sales orders can be cancelled.

## Customer Binding Arrangements and the Related Customer Relationships

- IE216. If an entity establishes relationships with its customers through binding arrangements, those customer relationships arise from binding arrangement rights. Therefore, customer binding arrangements and the related customer relationships acquired in an acquisition meet the binding arrangement criterion, even if confidentiality or other terms of the binding arrangement prohibit the sale or transfer of a binding arrangement separately from the acquired operation.
- IE217. A customer binding arrangement and the related customer relationship may represent two distinct intangible assets. Both the useful lives and the pattern in which the economic benefits of the two assets are consumed may differ.
- IE218. A customer relationship exists between an entity and its customer if (a) the entity has information about the customer and has regular contact with the customer and (b) the customer has the ability to make direct contact with the entity. Customer relationships meet the binding arrangement criterion if an entity has a practice of establishing binding arrangements with its customers, regardless of whether a binding arrangement exists at the acquisition date. Customer relationships may also arise through means other than binding arrangements, such as through regular contact by sales or service representatives.
- IE219. As noted in paragraph IE215, an order or a production backlog arises from binding arrangements such as purchase or sales orders and is therefore considered a binding arrangement right. Consequently, if an entity has relationships with its customers through these types of binding arrangements, the customer relationships also arise from binding arrangement rights and therefore meet the binding arrangement criterion.

## Examples

IE220. The following examples illustrate the recognition of customer binding arrangement and customer relationship intangible assets acquired in an acquisition.

- (a) Acquirer Entity (AE) acquires Target Entity (TE) in an acquisition on 31 December 20X5. TE has a five-year agreement to supply goods to Customer. Both TE and AE believe that Customer will renew the agreement at the end of the current binding arrangement. The agreement is not separable.

The agreement, whether cancellable or not, meets the binding arrangement criterion. Additionally, because TE establishes its relationship with Customer through a binding arrangement, not only the agreement itself but also TE's customer relationship with Customer meet the binding arrangement criterion.

- (b) AE acquires TE in an acquisition on 31 December 20X5. TE manufactures goods in two distinct lines of business: sporting goods and electronics. Customer purchases both sporting goods and electronics from TE. TE has a binding arrangement with Customer to be its exclusive provider of sporting goods but has no binding arrangement for the supply of electronics to Customer. Both TE and AE believe that only one overall customer relationship exists between TE and Customer.

The binding arrangement to be Customer's exclusive supplier of sporting goods, whether cancellable or not, meets the binding arrangement criterion. Additionally, because TE establishes its relationship with Customer through a binding arrangement, the customer relationship with Customer meets the binding arrangement criterion. Because TE has only one customer relationship with Customer, the fair value of that relationship incorporates assumptions about TE's relationship with Customer related to both sporting goods and electronics. However, if AE determines that the customer relationships with Customer for sporting goods and for electronics are separate from each other, AE would assess whether the customer relationship for electronics meets the separability criterion for identification as an intangible asset.

- (c) AE acquires TE in an acquisition on 31 December 20X5. TE does business with its customers solely through purchase and sales orders. At 31 December 20X5, TE has a backlog of customer purchase orders from 60 percent of its customers, all of whom are recurring customers. The other 40 percent of TE's customers are also recurring customers. However, as of 31 December 20X5, TE has no open purchase orders or other binding arrangements with those customers.

Regardless of whether they are cancellable or not, the purchase orders from 60 percent of TE's customers meet the binding arrangement criterion. Additionally, because TE has established its relationship with 60 percent of its customers through binding arrangements, not only the purchase orders but also TE's customer relationships meet the binding arrangement criterion. Because TE has a practice of establishing binding arrangements with the remaining 40 percent of its customers, its relationship with those customers also arises through binding arrangement rights and therefore meets the binding arrangement criterion even though TE does not have binding arrangements with those customers at 31 December 20X5.

- (d) AE acquires TE, an insurer, in an acquisition on 31 December 20X5. TE has a portfolio of one-year motor insurance contracts that are cancellable by policyholders.

Because TE establishes its relationships with policyholders through insurance contracts, the customer relationship with policyholders meets the binding arrangement criterion. PBE IPSAS 26 *Impairment of Cash-Generating Assets* and PBE IPSAS 31 *Intangible Assets* apply to the customer relationship intangible asset.

## Customer Relationships arising through Means other than Binding Arrangements

IE221. A customer relationship acquired in an acquisition that does not arise from a binding arrangement may nevertheless be identifiable because the relationship is separable. Exchange transactions for the same asset or a similar asset that indicate that other entities have sold or otherwise transferred a particular type of customer relationship arising through means other than binding arrangements would provide evidence that the relationship is separable.

*Artistic-Related Intangible Assets*

IE222. Examples of artistic-related intangible assets are:

<b>Class</b>	<b>Basis</b>
Plays, operas and ballets	Binding arrangement
Books, magazines, newspapers and other literary works	Binding arrangement
Musical works such as compositions, song lyrics and advertising jingles	Binding arrangement
Pictures and photographs	Binding arrangement
Video and audio-visual material, including motion pictures or films, music videos and television programmes	Binding arrangement

IE223. Artistic-related assets acquired in an acquisition are identifiable if they arise from binding arrangements (including rights from contracts) or legal rights such as those provided by copyright. The holder can transfer a copyright, either in whole through an assignment or in part through a licensing agreement. An acquirer is not precluded from recognising a copyright intangible asset and any related assignments or licence agreements as a single asset, provided they have similar useful lives.

*Binding Arrangement-Based Intangible Assets*

IE224. Binding arrangement-based intangible assets represent the value of rights that arise from binding arrangements. Binding arrangements with customers are one type of binding arrangement-based intangible asset. If the terms of a binding arrangement give rise to a liability (for example, if the terms of an operating lease or binding arrangement with a customer are unfavourable relative to market terms), the acquirer recognises it as a liability assumed in the acquisition. Examples of binding arrangement-based intangible assets are:

<b>Class</b>	<b>Basis</b>
Licensing, royalty and standstill agreements	Binding arrangement
Advertising, construction, management, service or supply binding arrangements	Binding arrangement
Lease agreements (whether the acquired operation is the lessee or the lessor)	Binding arrangement
Construction permits	Binding arrangement
Franchise agreements	Binding arrangement
Operating and broadcast rights	Binding arrangement
Servicing binding arrangements, such as mortgage servicing binding arrangements	Binding arrangement
Binding arrangements for employment	Binding arrangement
Use rights, such as drilling, water, air, timber cutting and route authorities	Binding arrangement

## Servicing Binding Arrangements, such as Mortgage Servicing Binding Arrangements

- IE225. Binding arrangements to service financial assets are one type of binding arrangement-based intangible asset. Although servicing is inherent in all financial assets, it becomes a distinct asset (or liability) by one of the following:
- (a) When separated in the binding arrangement from the underlying financial asset by sale or securitisation of the assets with servicing retained;
  - (b) Through the separate purchase and assumption of the servicing.
- IE226. If mortgage loans, credit card receivables or other financial assets are acquired in an acquisition with servicing retained, the inherent servicing rights are not a separate intangible asset because the fair value of those servicing rights is included in the measurement of the fair value of the acquired financial asset.

## Binding Arrangements for Employment

- IE227. Binding arrangements for employment that are beneficial binding arrangements from the perspective of the employer because the pricing of those binding arrangements is favourable relative to market terms are one type of binding arrangement-based intangible asset.

## Use Rights

- IE228. Use rights include rights for drilling, water, air, timber cutting and route authorities. Some use rights are binding arrangement-based intangible assets to be accounted for separately from goodwill. Other use rights may have characteristics of tangible assets rather than of intangible assets. An acquirer should account for use rights on the basis of their nature.

*Technology-Based Intangible Assets*

- IE229. Examples of technology-based intangible assets are:

<b>Class</b>	<b>Basis</b>
Patented technology	Binding arrangement
Computer software and mask works	Binding arrangement
Unpatented technology	No binding arrangement
Databases, including title plants	No binding arrangement
Trade secrets, such as secret formulas, processes and recipes	Binding arrangement

## Computer Software and Mask Works

- IE230. Computer software and programme formats acquired in an acquisition that are protected legally, such as by patent or copyright, meet the binding arrangement criterion for identification as intangible assets.
- IE231. Mask works are software permanently stored on a read-only memory chip as a series of stencils or integrated circuitry. Mask works may have legal protection. Mask works with legal protection that are acquired in an acquisition meet the binding arrangement criterion for identification as intangible assets.

## Databases, Including Title Plants

- IE232. Databases are collections of information, often stored in electronic form (such as on computer disks or files). A database that includes original works of authorship may be entitled to copyright protection. A database acquired in an acquisition and protected by copyright meets the binding arrangement criterion. However, a database typically includes information created as a consequence of an entity's normal operations, such as lists of service users, or specialized information, such as scientific data or credit information. Databases that are not protected by copyright can be, and often are, exchanged, licensed or leased to others in their entirety or in part. Therefore, even if the future economic benefits from a database do not arise from legal rights, a database acquired in an acquisition meets the separability criterion.

- IE233. Title plants constitute a historical record of all matters affecting title to parcels of land in a particular geographical area. Title plant assets are bought and sold, either in whole or in part, in exchange transactions or are licensed. Therefore, title plant assets acquired in an acquisition meet the separability criterion.

Trade Secrets, such as Secret Formulas, Processes and Recipes

- IE234. A trade secret is 'information, including a formula, pattern, recipe, compilation, programme, device, method, technique, or process that (a) derives independent economic value, actual or potential, from not being generally known and (b) is the subject of efforts that are reasonable under the circumstances to maintain its secrecy.'<sup>13</sup> If the future economic benefits from a trade secret acquired in an acquisition are legally protected, that asset meets the binding arrangement criterion. Otherwise, trade secrets acquired in an acquisition are identifiable only if the separability criterion is met, which is likely to be the case.

### Measurement of Non-Controlling Interest (NCI) in an Acquisition

*Illustrating the Consequences of Applying Paragraph 73 of PBE IPSAS 40.*

- IE235. The following examples illustrate the measurement of components of NCI at the acquisition date in an acquisition.

*Measurement of NCI Including Preference Shares*

- IE236. TE has issued 100 preference shares, which are classified as equity. The preference shares have a nominal value of CU1 each. The preference shares give their holders a right to a preferential dividend in priority to the payment of any dividend to the holders of ordinary shares. Upon liquidation of TE, the holders of the preference shares are entitled to receive out of the assets available for distribution the amount of CU1 per share in priority to the holders of ordinary shares. The holders of the preference shares do not have any further rights on liquidation.
- IE237. AE acquires all ordinary shares of TE. The transaction gives AE control of TE, and an analysis of the economic substance of the combination using the guidance in paragraphs 9–14 and AG19–AG50 of PBE IPSAS 40 confirms the transaction is an acquisition. The acquisition-date fair value of the preference shares is CU120.
- IE238. Paragraph 73 of PBE IPSAS 40 states that for each acquisition, the acquirer shall measure at the acquisition date components of non-controlling interest in the acquired operation that are present ownership interests and entitle their holders to a proportionate share of the entity's net assets in the event of liquidation at either fair value or the present ownership instruments' proportionate share in the acquired operation's recognised amounts of the identifiable net assets. All other components of non-controlling interest must be measured at their acquisition-date fair value, unless another measurement basis is required by PBE Standards.
- IE239. The non-controlling interests that relate to TE's preference shares do not qualify for the measurement choice in paragraph 73 of PBE IPSAS 40 because they do not entitle their holders to a proportionate share of the entity's net assets in the event of liquidation. The acquirer measures the preference shares at their acquisition-date fair value of CU120.

*First Variation*

- IE240. Suppose that upon liquidation of TE, the preference shares entitle their holders to receive a proportionate share of the assets available for distribution. The holders of the preference shares have equal right and ranking to the holders of ordinary shares in the event of liquidation. Assume that the acquisition-date fair value of the preference shares is now CU160 and that the proportionate share of TE's recognised amounts of the identifiable net assets that is attributable to the preference shares is CU140.
- IE241. The preference shares qualify for the measurement choice in paragraph 73 of PBE IPSAS 40. AE can choose to measure the preference shares either at their acquisition-date fair value of CU160 or at their

<sup>13</sup> Melvin Simensky and Lanning Bryer, *The New Role of Intellectual Property in Commercial Transactions* (New York: John Wiley & Sons, 1998), page 293.

proportionate share in the acquired operation's recognised amounts of the identifiable net assets of CU140.

### *Second Variation*

- IE242. Suppose also that TE has issued share options as remuneration to its employees. The share options are classified as equity and are vested at the acquisition date. They do not represent present ownership interest and do not entitle their holders to a proportionate share of TE's net assets in the event of liquidation. The fair value of the share options in accordance with the relevant international or national accounting standard dealing with share-based payments at the acquisition date is CU200. The share options do not expire on the acquisition date and AE does not replace them.
- IE243. Paragraph 73 of PBE IPSAS 40 requires such share options to be measured at their acquisition-date fair value, unless another measurement basis is required by PBE Standards. Paragraph 84 of PBE IPSAS 40 states that the acquirer shall measure an equity instrument related to share-based payment transactions of the acquired operation in accordance with the relevant international or national accounting standard dealing with share-based payments.
- IE244. The acquirer measures the non-controlling interests that are related to the share options at their fair value of CU200.

### **Forgiveness of Amounts of Tax Due in an Acquisition**

*Illustrating the Consequences of Accounting for Tax Forgiveness in an Acquisition by Applying Paragraphs 78–79 and AG85 and AG87 of PBE IPSAS 40*

- IE245. The following example illustrates the accounting for an acquisition in which part of the acquired operation's tax liability is forgiven as part of the terms of the acquisition.
- IE246. On 1 January 20X4 AE, a government ministry acting on behalf of the government, acquires TE, a private entity in exchange for cash of CU575. As a result of the acquisition, AE expects to reduce costs through economies of scale. The fair value of the assets acquired and liabilities assumed are as follows:

<b>Assets acquired and liabilities assumed:</b>	<b>CU</b>
Financial assets	265
Inventory	5
Property, plant and equipment	640
Identifiable intangible assets	12
Financial liabilities	(320)
Tax liabilities	(40)
Total net assets	562

- IE247. AE recognises goodwill of CU13, the difference between the price paid to acquire TE (CU575) and the net assets of TE (CU562).

- IE248. Suppose that as part of the terms of the acquisition, the government requires MF (the tax authority) to forgive 50 percent of TE's tax liability. The fair value of the assets acquired and liabilities assumed would now be as follows:

<b>Assets acquired and liabilities assumed:</b>	<b>CU</b>
Financial assets	265
Inventory	5
Property, plant and equipment	640
Identifiable intangible assets	12
Financial liabilities	(320)
Tax liabilities	(20)
Total net assets	582

- IE249. AE recognises a gain of CU7, the difference between the price paid to acquire TE (CU575) and the net assets of TE (CU582). AE would account for the remaining tax liability in accordance with PBE IAS 12~~the relevant international or national accounting standard~~ dealing with income taxes.
- IE250. MF would recognise an adjustment for the tax forgiven, and accounts for the remaining tax receivable in accordance with PBE IPSAS 23,~~and would recognise an adjustment for the tax forgiven.~~

Agenda item 7.1 reference: Tax forgiven (paras 22–27)
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### Gain on a Bargain Purchase in an Acquisition

*Illustrating the Consequences of Recognising and Measuring a Gain from a Bargain Purchase in an Acquisition by Applying Paragraphs 85–90 of PBE IPSAS 40*

- IE251. The following example illustrates the accounting for an acquisition in which a gain on a bargain purchase is recognised.
- IE252. On 1 January 20X5 AE acquires 80 percent of the equity interests of TE, a private entity, in exchange for cash of CU150. Because the former owners of TE needed to dispose of their investments in TE by a specified date, they did not have sufficient time to market TE to multiple potential buyers. The management of AE initially measures the separately recognizable identifiable assets acquired and the liabilities assumed as of the acquisition date in accordance with the requirements of PBE IPSAS 40. The identifiable assets are measured at CU250 and the liabilities assumed are measured at CU50. AE engages an independent consultant, who determines that the fair value of the 20 percent non-controlling interest in TE is CU42.
- IE253. The amount of TE's identifiable net assets (CU200, calculated as CU250 – CU50) exceeds the fair value of the consideration transferred plus the fair value of the non-controlling interest in TE. Therefore, AE reviews the procedures it used to identify and measure the assets acquired and liabilities assumed and to measure the fair value of both the non-controlling interest in TE and the consideration

transferred. After that review, AE decides that the procedures and resulting measures were appropriate. AE measures the gain on its purchase of the 80 percent interest as follows:

		CU
Amount of the identifiable net assets acquired (CU250 – CU50)		200
Less: Fair value of the consideration transferred for AE's 80 percent interest in TE; plus	150	
Fair value of non-controlling interest in TE	42	
		192
Gain on bargain purchase of 80 percent interest		8
IE254. AE would record its acquisition of TE in its consolidated financial statements as follows:		

	CU	CU
Dr Identifiable assets acquired	250	
Cr Cash		150
Cr Liabilities assumed		50
Cr Gain on the bargain purchase		8
Cr Equity—non-controlling interest in TE		42

- IE255. If the acquirer chose to measure the non-controlling interest in TE on the basis of its proportionate interest in the identifiable net assets of the acquired operation, the recognised amount of the non-controlling interest would be CU40 ( $\text{CU}200 \times 0.20$ ). The gain on the bargain purchase then would be CU10 ( $\text{CU}200 - (\text{CU}150 + \text{CU}40)$ ).

### Measurement Period in an Acquisition

*Illustrating the Consequences of Applying Paragraphs 103–108 of PBE IPSAS 40.*

- IE256. If the initial accounting for an acquisition is not complete at the end of the financial reporting period in which the combination occurs, paragraph 103 of PBE IPSAS 40 requires the acquirer to recognise in its financial statements provisional amounts for the items for which the accounting is incomplete. During the measurement period, the acquirer recognises adjustments to the provisional amounts needed to reflect new information obtained about facts and circumstances that existed as of the acquisition date and, if known, would have affected the measurement of the amounts recognised as of that date. Paragraph 107 of PBE IPSAS 40 requires the acquirer to recognise such adjustments as if the accounting for the acquisition had been completed at the acquisition date. Measurement period adjustments are not included in surplus or deficit.
- IE257. Suppose that AE acquires TE on 30 September 20X7. AE seeks an independent valuation for an item of property, plant and equipment acquired in the combination, and the valuation was not complete by the time AE authorised for issue its financial statements for the year ended 31 December 20X7. In its 20X7 annual financial statements, AE recognised a provisional fair value for the asset of CU30,000. At the acquisition date, the item of property, plant and equipment had a remaining useful life of five years. Five months after the acquisition date, AE received the independent valuation, which estimated the asset's acquisition-date fair value as CU40,000.



- IE258. In its financial statements for the year ended 31 December 20X8, AE retrospectively adjusts the 20X7 prior year information as follows:
- (a) The carrying amount of property, plant and equipment as of 31 December 20X7 is increased by CU9,500. That adjustment is measured as the fair value adjustment at the acquisition date of CU10,000 less the additional depreciation that would have been recognised if the asset's fair value at the acquisition date had been recognised from that date (CU500 for three months' depreciation).
  - (b) The carrying amount of goodwill as of 31 December 20X7 is decreased by CU10,000.
  - (c) Depreciation expense for 20X7 is increased by CU500.
- IE259. In accordance with paragraph 124 of PBE IPSAS 40, AE discloses:
- (a) In its 20X7 financial statements, that the initial accounting for the acquisition has not been completed because the valuation of property, plant and equipment has not yet been received.
  - (b) In its 20X8 financial statements, the amounts and explanations of the adjustments to the provisional values recognised during the current reporting period. Therefore, AE discloses that the 20X7 comparative information is adjusted retrospectively to increase the fair value of the item of property, plant and equipment at the acquisition date by CU9,500, offset by a decrease to goodwill of CU10,000 and an increase in depreciation expense of CU500.

### **Determining what is Part of the Acquisition Transaction**

#### *Settlement of a Pre-Existing Relationship —Loan*

##### *Illustrating the Consequences of Applying Paragraphs 109–110 and AG98–AG101 of PBE IPSAS 40.*

- IE260. AE provides TE with a five year, fixed rate loan of CU100. Interest is payable quarterly, with the principal repaid on maturity. With two years remaining under the loan agreement, AE acquires TE.
- IE261. Included in the total fair value of TE is a CU90 financial liability for the fair value of the loan arrangement with AE. At the acquisition date, the carrying amount of the corresponding financial asset in AE's financial statements (the amortized cost of the loan) is CU100.
- IE262. In this example, AE calculates a loss of CU10. The loss is calculated as the difference between the fair value of the financial liability assumed and carrying amount of the corresponding financial asset previously recognised by AE. In its consolidated financial statements, AE will eliminate its financial asset (CU100) against the fair value of TE's financial liability (CU90), the difference representing the loss to AE.

#### *Settlement of a Pre-Existing Relationship —Transfers*

##### *Illustrating the Consequences of Applying Paragraphs 109–110 and AG98–AG101 of PBE IPSAS 40.*

- IE263. On 1 January 20X7, AE acquires TE. Previously, on 1 October 20X6, AE provided TE with a grant of CU800 to be used in the provision of an agreed number of training courses.
- IE264. The grant was subject to a condition that the grant would be returned proportionately to the number of training courses not delivered. At the acquisition date, TE had delivered a quarter of the agreed number of courses, and recognised a liability of CU600 in respect of its performance obligation, in accordance with PBE IPSAS 23. Based on past experience, AE considered that TE was more likely than not to deliver the training courses. It was therefore not probable that there would be a flow of resources to AE, and AE did not recognise an asset in respect of the grant, but accounted for the full CU800 as an expense.
- IE265. In this example, AE calculates a gain of CU600. The gain is calculated as the liability assumed that is derecognised because, as a result of the acquisition, there is no longer an obligation owed to a third party.
- IE266. In this example, no corresponding asset had been recognised by AE; if AE had previously recognised a corresponding asset, this would be derecognised at the acquisition date, and the derecognised amount would be included in the calculation of the gain or loss.

*Settlement of a Pre-Existing Relationship —Supply Contract**Illustrating the Consequences of Applying Paragraphs 109–110 and AG98–AG101 of PBE IPSAS 40.*

- IE267. AE purchases electronic components from TE under a five-year supply contract at fixed rates. Currently, the fixed rates are higher than the rates at which AE could purchase similar electronic components from another supplier. The supply contract allows AE to terminate the contract before the end of the initial five-year term but only by paying a CU6 million penalty. With three years remaining under the supply contract, AE pays CU50 million to acquire TE, which is the fair value of TE based on what other market participants would be willing to pay.
- IE268. Included in the total fair value of TE is CU8 million related to the fair value of the supply contract with AE. The CU8 million represents a CU3 million component that is ‘at market’ because the pricing is comparable to pricing for current market transactions for the same or similar items (selling effort, customer relationships and so on) and a CU5 million component for pricing that is unfavourable to AE because it exceeds the price of current market transactions for similar items. TE has no other identifiable assets or liabilities related to the supply contract, and AE has not recognised any assets or liabilities related to the supply contract before the acquisition.
- IE269. In this example, AE calculates a loss of CU5 million (the lesser of the CU6 million stated settlement amount and the amount by which the contract is unfavourable to the acquirer) separately from the acquisition. The CU3 million ‘at-market’ component of the contract is part of goodwill.
- IE270. Whether AE had recognised previously an amount in its financial statements related to a pre-existing relationship will affect the amount recognised as a gain or loss for the effective settlement of the relationship. Suppose that PBE Standards had required AE to recognise a CU6 million liability for the supply contract before the acquisition. In that situation, AE recognises a CU1 million settlement gain on the contract in surplus or deficit at the acquisition date (the CU5 million measured loss on the contract less the CU6 million loss previously recognised). In other words, AE has in effect settled a recognised liability of CU6 million for CU5 million, resulting in a gain of CU1 million.

*Contingent Payments to Employees in an Acquisition**Illustrating the Consequences of Applying Paragraphs 109–110, AG98 and AG102–AG103 of PBE IPSAS 40.*

- IE271. TE appointed a candidate as its new CEO under a ten-year contract. The contract required TE to pay the candidate CU5 million if TE is acquired before the contract expires. AE acquires TE eight years later. The CEO was still employed at the acquisition date and will receive the additional payment under the existing contract.
- IE272. In this example, TE entered into the employment agreement before the negotiations of the combination began, and the purpose of the agreement was to obtain the services of CEO. Thus, there is no evidence that the agreement was arranged primarily to provide benefits to AE or the combined entity. Therefore, the liability to pay CU5 million is included in the application of the acquisition method.
- IE273. In other circumstances, TE might enter into a similar agreement with CEO at the suggestion of AE during the negotiations for the acquisition. If so, the primary purpose of the agreement might be to provide severance pay to CEO, and the agreement may primarily benefit AE or the combined entity rather than TE or its former owners. In that situation, AE accounts for the liability to pay CEO in its post-combination financial statements separately from application of the acquisition method.

**Subsequent Measurement of Transfers, Concessionary Loans and Similar Benefits Received by an Acquirer or an Acquired Operation on the Basis of Criteria that may Change as a Result of an Acquisition***Illustrating the Consequences of Applying Paragraphs 114 and AG109–AG111 of PBE IPSAS 40.*

- IE274. The following example illustrates the subsequent accounting for a transfer received by an acquirer on the basis of criteria that may change as a result of an acquisition.
- IE275. On 1 January 20X6, a national government provides an annual grant to those municipalities where their revenue per head of population is below a threshold. On 1 June 20X3 AE, a municipality, acquires TE, a shopping complex that will generate revenue for AE. AE had previously received a grant of CU500, based on its revenue per head of population.

- IE276. As a result of its acquisition of TE on 1 June 20X3, the revenue per head of population of AE increases above the threshold that the government had set when allocating grants.
- IE277. On 1 July 20X3, the national government requires AE to repay a portion (CU100) of the grant previously received by AE. AE recognises a liability and an expense of CU100 on 1 July 20X3.

### Disclosure Requirements Relating to Acquisitions

*Illustrating the Consequences of Applying the Disclosure Requirements in Paragraphs 119–125 of PBE IPSAS 40.*

- IE278. The following example illustrates some of the disclosure requirements relating to acquisitions; it is not based on an actual transaction. The example assumes that AE is a public sector entity with responsibility for healthcare in its region and that TE is a listed entity. The illustration presents the disclosures in a tabular format that refers to the specific disclosure requirements illustrated. An actual footnote might present many of the disclosures illustrated in a simple narrative format.

#### Paragraph reference

- 120(a)–(d) On 30 June 20X2 AE acquired 75 percent of the ordinary shares of TE and obtained control of TE. An analysis of the economic substance of the combination confirms the transaction is an acquisition. TE is a provider of medical supplies. As a result of the acquisition, AE is expected to deliver improved healthcare to its residents. It also expects to reduce costs through economies of scale.
- 120(e) The goodwill of CU2,500 arising from the acquisition consists largely of the synergies and economies of scale expected from combining the operations of AE and TE.
- 120(k) None of the goodwill recognised is expected to be deductible for income tax purposes. The following table summarizes the consideration paid for TE and the amounts of the assets acquired and liabilities assumed recognised at the acquisition date, as well as the fair value at the acquisition date of the non-controlling interest in TE.

#### At 30 June 20X2

	Consideration	CU
120(f)(i)	Cash	11,000
120(f)(iii); 120(g)(i)	Contingent consideration arrangement	1,000
120(f)	<b>Total consideration transferred</b>	<b>12,000</b>
120(m)	<b>Acquisition-related costs</b> (included in selling, general and administrative expenses in AE's statement of comprehensive income for the year ended 31 December 20X2)	1,250
120(i)	<b>Recognised amounts of identifiable assets acquired and liabilities assumed</b>	
	Financial assets	3,500
	Inventory	1,000
	Property, plant and equipment	10,000

**Paragraph  
reference**

	Identifiable intangible assets	3,300
	Financial liabilities	(4,000)
	Contingent liability	(1,000)
	Total identifiable net assets	12,800
120(p)(i)	<b>Non-controlling interest in TE</b>	(3,300)
	<b>Goodwill</b>	2,500
		12,000
120(f)(iii)	<p>The contingent consideration arrangement requires AE to pay the former owners of TE 5 percent of the revenues of XE, an unconsolidated equity investment owned by TE, in excess of CU7,500 for 20X3, up to a maximum amount of CU2,500 (undiscounted).</p> <p>The potential undiscounted amount of all future payments that AE could be required to make under the contingent consideration arrangement is between CU0 and CU2,500.</p> <p>The fair value of the contingent consideration arrangement of CU1,000 was estimated by applying an income approach. Key assumptions include a discount rate range of 20–25 percent and assumed probability-adjusted revenues in XE of CU10,000–20,000.</p> <p>As of 31 December 20X2, neither the amount recognised for the contingent consideration arrangement, nor the range of outcomes or the assumptions used to develop the estimates had changed.</p>	
120(g)		
124(b)		
120(h)	<p>The fair value of the financial assets acquired includes receivables with a fair value of CU2,375. The gross amount due under the contracts is CU3,100, of which CU450 is expected to be uncollectible.</p>	
124(a)	<p>The fair value of the acquired identifiable intangible assets of CU3,300 is provisional pending receipt of the final valuations for those assets.</p>	
120(j)	<p>A contingent liability of CU1,000 has been recognised for expected warranty claims on products sold by TE during the last three years. We expect that the majority of this expenditure will be incurred in 20X3 and that all will be incurred by the end of 20X4.</p> <p>The potential undiscounted amount of all future payments that AE could be required to make under the warranty arrangements is estimated to be between CU500 and CU1,500. As of 31 December 20X2, there has been no change since 30 June 20X2 in the amount recognised for the liability or any change in the range of outcomes or assumptions used to develop the estimates.</p>	
124(c)		
PBE IPSAS 19 .97, 98		
120(p)	<p>The fair value of the non-controlling interest in TE, a listed entity, was measured using the closing market price of TE's ordinary shares on the acquisition date.</p>	
120(r)(i)	<p>The revenue included in the consolidated statement of comprehensive income since 30 June 20X2 contributed by TE was CU4,090. TE also contributed profit of CU1,710 over the same period.</p>	
120(r)(ii)	<p>Had TE been consolidated from 1 January 20X2 the consolidated statement of comprehensive income would have included revenue of CU27,670 and profit of CU12,870.</p>	

In considering the disclosures related to an acquisition, an entity may find it helpful to refer to the discussion of materiality in PBE IPSAS 1.

## Comparison with IPSAS 40

PBE IPSAS 40 **PBE** *Combinations* is drawn from IPSAS 40 *Public Sector Combinations*.

The significant differences between PBE IPSAS 40 and IPSAS 40 are:

- (a) PBE Standards require the presentation of a statement of comprehensive revenue and expense. IPSASs require the presentation of a statement of financial performance.

## History of Amendments

PBE IPSAS 40 *PBE Combinations* was issued in [date].

This table lists the pronouncements establishing and substantially amending PBE IPSAS 40.

Pronouncements	Date approved	Early operative date	Effective date (annual reporting periods... on or after ...)
PBE IPSAS 40 <i>PBE Combinations</i>	[date]	Early application is permitted	[date]



NZ ACCOUNTING  
STANDARDS  
BOARD

## Memorandum

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**Date:** 1 September 2017

**To:** NZASB Members

**From:** Judith Pinny

**Subject:** IPSASB Consultation Paper *Financial Reporting for Heritage in the Public Sector*

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### Action required<sup>1</sup>

1. The Board is asked to CONSIDER and APPROVE the draft comment letter to the IPSASB on the Consultation Paper *Financial Reporting for Heritage in the Public Sector* (the CP).

### Background

2. The IPSASB issued the CP in April 2017. Comments were due to the NZASB by 18 August 2017, and are due to the IPSASB by 30 September 2017.
3. We have undertaken the following steps in developing this draft comment letter.
  - (a) 21 June 2017: Sought NZASB's initial views.
  - (b) June/July 2017: Held outreach events in Auckland, Wellington and Christchurch to seek feedback from museums and other interested parties.
  - (c) 2 August 2017: Reported back on outreach, one submission received and staff sought NZASB's feedback on the draft comment letter.
  - (d) August 2017: Board sub-committee provided feedback on the updated draft comment letter which incorporated comments from the August Board meeting.
  - (e) 31 August 2017: Further submissions received and comments incorporated in current draft comment letter (agenda item 8.2).

### Structure of this memo

4. The remainder of this memo is structured as follows:
  - (a) summary of proposals in the CP;
  - (b) draft comment letter;
  - (c) recommendations; and

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<sup>1</sup> This memo refers to the work of the International Accounting Standards Board (IASB) and uses registered trademarks of the IFRS Foundation (for example, IFRS® Standards, IFRIC® Interpretations and IASB® papers).

- (d) next steps.

### Summary of proposals in the CP

5. The CP describes heritage items as items that are intended to be held indefinitely and preserved for the benefit of present and future generations because of their rarity and/or significance.
6. The CP proposes that:
  - (a) heritage items' special characteristics do not prevent them from being assets for the purposes of financial reporting;
  - (b) heritage items should be recognised in the statement of financial position if they meet the recognition criteria in the IPSASB's *Conceptual Framework for General Purpose Financial Reporting by Public Sector Entities* (IPSASB's Conceptual Framework); and
  - (c) in many cases, it will be possible to assign a monetary value to heritage assets.
7. It also discusses:
  - (a) initial and subsequent measurement of heritage assets;
  - (b) whether heritage preservation responsibilities could involve present obligations for entities, which should be recognised as liabilities in the financial statements; and
  - (c) presentation<sup>2</sup> of information for heritage in general purpose financial statements.

### Draft comment letter

8. At the August NZASB meeting, the Board provided feedback on an earlier draft of this comment letter and considered one submission (agenda item 8.3).
9. The updated draft comment letter incorporates comments received during the discussion at the August Board meeting, and submissions received since that meeting (agenda items 2.3.5, 2.3.6, 8.3.1 and 8.3.2).

### Recommendations

10. We recommend that the Board CONSIDERS and APPROVES the draft comment letter in agenda item 8.2.

### Next steps

11. We intend to finalise the comment letter soon after the September Board meeting so that it reaches the IPSASB in time for the 30 September due date.

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<sup>2</sup> The IPSASB's concept of *presentation* includes both information disclosed on the face of the financial statements and information disclosed in the notes.



**Attachments**

Agenda item 8.2: Draft comment letter

Submissions received

Agenda item 2.3.5: CA ANZ Draft submission to IPSASB

Agenda item 2.3.6: OAG Final submission to IPSASB

Agenda item 8.3: New Zealand Police Museum (supporting papers)

Agenda item 8.3.1: Informal Comments – Respondent 1

Agenda item 8.3.2: Informal Comments – Respondent 2

IPSASB Documents

Agenda item 8.4: IPSASB CP *Financial Reporting for Heritage in the Public Sector – At a Glance* (supporting papers)

Agenda item 8.5: IPSASB CP *Financial Reporting for Heritage in the Public Sector* (supporting papers)



NZ ACCOUNTING  
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Xx September 2017

Mr John Stanford  
Technical Director  
International Public Sector Accounting Standards Board  
International Federation of Accountants  
277 Wellington Street West  
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**CANADA**  
Submitted to: [www.ifac.org](http://www.ifac.org)

Dear John

**Consultation Paper *Financial Reporting for Heritage in the Public Sector***

Thank you for the opportunity to comment on the Consultation Paper *Financial Reporting for Heritage in the Public Sector* (CP). The CP has been exposed in New Zealand and some New Zealand constituents may have made comments directly to you.

To put our response to you in context, there is one significant difference between our current New Zealand standard, PBE IPSAS 17 *Property, Plant and Equipment* and IPSAS 17 *Property, Plant and Equipment*. PBE IPSAS 17 requires that heritage assets which meet the recognition requirements be recognised as property, plant and equipment when they can be reliably measured. PBE IPSAS 31 *Intangible Assets* takes a similar approach to PBE IPSAS 17. The requirement to recognise heritage assets in the statement of financial position has been mandated in our New Zealand accounting standards for many years.

When developing PBE IPSAS 17 the New Zealand Accounting Standards Board (NZASB) noted there are instances where heritage assets are not able to be reliably measured and are therefore not recognised in the statement of financial position. The NZASB agreed that although non-recognition of heritage in such circumstances is appropriate, heritage assets should be recognised when they can be reliably measured.

We note that, notwithstanding the measurement challenges for heritage items, many New Zealand public benefit entities, both in the public sector and not-for-profit sector, have managed to establish values for financial reporting purposes under PBE IPSAS 17.

We acknowledge that financial statements have limitations and that valuations used for financial reporting have limitations. Financial statements are not the sole source of information for decision making and accountability. There will be other valuations used for other purposes and a role for additional information about heritage items, possibly in the financial statements, but also in service performance information or other reports. Despite the limitations of financial statements and the measurement of items for financial reporting purposes, this does not stop us from striving for completeness in financial reporting when the recognition requirements are satisfied.

We have undertaken constituent outreach on the CP, by facilitating roundtables in Wellington, Auckland and Christchurch. We have also received three written submissions, one from a museum, one from a museum umbrella entity and one from an academic. We also understand that the New Zealand membership body, Chartered Accountants Australia New Zealand, and the Office of the Auditor-General are making submissions directly to you.

Overall, we support the proposals in the CP to develop principles and requirements for the accounting for Heritage items. In addition, we recommend that the IPSASB develop non-mandatory general guidance to support the recognition and measurement requirements that already exist in IPSAS 17 and IPSAS 31 for heritage assets that meet the recognition criteria in the IPSASB's Conceptual Framework.

However, our outreach provided a unanimous view from constituents, which the NZASB concurs with, that the nominal cost of one currency unit is not an appropriate measurement basis for heritage assets. This approach would not promote consistent measurement practices and would likely be perceived as offensive and culturally insensitive, given the New Zealand view of heritage.

The unique characteristics of Māori heritage items in New Zealand can be particularly problematic when applying the recognition and measurement principles for accounting purposes. The Māori people see themselves as custodians of Māori heritage for past, present and future generations. This is different to the one-dimensional concept of control that is the accounting concept. Although a Māori heritage item may reside in a museum, ownership is still usually attributed to the Māori people. Furthermore, attributing any monetary value to an item of Māori heritage can be offensive to the Māori people. We have considered these Māori heritage matters in formulating our response to you.

Our recommendations and responses to the Specific Matters for Comment and Preliminary Views are set out in the Appendix 1 to this letter. If you have any queries or require clarification of any matters in this letter, please contact Judith Pinny ([Judith.pinny@xrb.govt.nz](mailto:Judith.pinny@xrb.govt.nz)) or me.

Yours sincerely

Kimberley Crook  
**Chair – New Zealand Accounting Standards Board**

## Appendix 1: Responses to Specific Questions for Comment and Preliminary Views in the Consultation Paper

### 1. Specific Matters for Comment – Chapter 1 (following paragraph 1.8)

Do you agree the IPSASB has captured all of the characteristics of heritage items and the potential consequences for financial reporting in paragraphs 1.7 and 1.8?

If not, please give reasons and identify any additional characteristics that you consider relevant.

The NZASB agrees with the heritage item characteristics identified by the IPSASB and the areas where these characteristics might have financial reporting consequences.

### 2. Preliminary View – Chapter 2.1 (following paragraph 2.11)

For the purposes of this CP, the following description reflects the special characteristics of heritage items and distinguishes them from other phenomena for the purposes of financial reporting:

Heritage items are items that are intended to be held indefinitely and preserved for the benefit of present and future generations because of their rarity and/or significance in relation, but not limited to, their archeological, architectural, agricultural, artistic, cultural, environmental, historical, natural, scientific or technological features.

Do you agree with the IPSASB's Preliminary View? If not, please provide your reasons.

In principle, the scope of the description of heritage items appears satisfactory. We note that this is a description of all heritage items, of which those heritage items that can be recognised as assets and measured for financial reporting purposes is a subset.

We recommend that the IPSASB consider adding "social" to the description of heritage items.

Heritage New Zealand<sup>1</sup>, which has Māori<sup>2</sup> heritage and national historic landmarks within its mandate, includes aesthetic, social, and traditional values within its definition of historical and cultural heritage.<sup>3</sup> One constituent suggested that "social heritage" be added to the definition of heritage items to capture all items of heritage significance to New Zealand. The reference to "social" can reflect a wider scope than cultural features. For example, some historic vehicles are considered to have social importance due to their impact on New Zealand society, but may not necessarily be considered to have cultural importance.

We consider it important that any definition used by the IPSASB explicitly emphasise that it is for financial reporting purposes, because there are many different views internationally on what is meant by "heritage".

<sup>1</sup> Heritage New Zealand is the New Zealand Government's expert advisor on historical and cultural heritage.

<sup>2</sup> The native people of New Zealand.

<sup>3</sup> <http://www.heritage.org.nz/resources/-/media/e0dde159aaef4d01b322f9d10d72b6ec.ashx>, page 6.

### 3. Preliminary View – Chapter 2.2 (following paragraph 2.12)

For the purposes of this CP, natural heritage covers areas and features, but excludes living plants and organisms that occupy or visit those areas or features.

Do you agree with the IPSASB's Preliminary View? If not, please provide your reasons.

The NZASB agrees that natural heritage covers areas and features.

However, the NZASB does not necessarily agree that natural heritage should specifically exclude living plants and organisms from the scope of heritage items. It is difficult to form a definitive conclusion without understanding:

- (a) the implications of including or excluding particular items; and
- (b) the unit of account to be applied (i.e. the species or the individual plant/organism).

Living plants and organisms could, in some instances, be recognised as heritage assets when they meet the recognition criteria in the Conceptual Framework. For example, in New Zealand endangered species are often held in protected areas (within natural heritage sites) and are individually tagged. For these individual protected animals, there may be instances where control can be demonstrated and the recognition criteria satisfied. The kiwi, a native bird, and the tuatara, a native three-eyed lizard, are considered to be heritage animals in New Zealand.

Another example provided during outreach events was the native Kauri trees in New Zealand. The Kauri trees are, in some cases, thousands of years old which would fulfil the "longevity criteria". The Kauris are both rare and significant to New Zealanders, and particularly the Māori people, but are excluded from the description of natural heritage used within the CP.

Historical items of this nature could, under specific circumstances, meet the current requirements for recognition as property, plant and equipment.

We consider that in many instances living plant and organisms will not meet the asset recognition criteria in the Conceptual Framework. However, this should not necessarily preclude them from the scope of heritage items for disclosure purposes. The inclusion of living plants and organisms within the scope of heritage items will encourage entities to acknowledge the significance and importance of these heritage items in their financial statements through disclosures, when not recognised as assets. Information about unrecognised heritage assets, for which an entity has custodian and preservation obligations, would be useful in the financial statements or in the service performance information.

### 4. Preliminary View – Chapter 3 (following paragraph 3.11)

The special characteristics of heritage items do not prevent them from being considered as assets for the purposes of financial reporting.

Do you agree with the IPSASB's Preliminary View? If not, please provide your reasons.

We agree that the special characteristics of heritage items do not prevent them from being considered as assets for financial reporting purposes.

The New Zealand PBE Standards, PBE IPSAS 17 and PBE IPSAS 31, require recognition and measurement of heritage assets. The requirements in PBE IPSAS 17 and PBE IPSAS 31 differ from the IPSASB's current requirements in IPSAS 17 and IPSAS 31.

For many years NZ GAAP has required that entities recognise and measure heritage assets in the same way as other items of property, plant and equipment when the asset recognition criteria are met.

The NZASB notes that there are instances where heritage assets are not able to be reliably measured and therefore not recognised in the statement of financial position. Although non-recognition of heritage in such circumstances is appropriate, heritage assets should be recognised when they can be reliably measured.

**5. Specific Matters for Comment – Chapter 4.1 (following paragraph 4.17)**

Do you support initially recognising heritage assets at a nominal cost of one currency unit where historical cost is zero, such as when a fully depreciated asset is categorised as a heritage asset then transferred to a museum at no consideration, or an entity obtains a natural heritage asset without consideration?

If so, provide your reasons.

In providing our response below, we have focused on the appropriate accounting treatment for an entity that is already applying IPSAS (i.e. not a first-time adopter of IPSAS) and the appropriate treatment on an on-going basis (i.e. not on first-time application of a new standard requiring recognition of heritage assets for the first time). We consider that transitional provisions (including whether any pragmatic relief should be provided to entities that have not recognised heritage assets previously) should be considered separately.

The NZASB does not support the recognition of heritage assets at one currency unit. Although this maybe a pragmatic solution, we believe that perceptions about ascribing notional values are likely to vary across jurisdictions, and could be regarded as culturally insensitive. Our discussions with the Māori people about Heritage has confirmed that this is the case in New Zealand.

We note that the recognition criteria in the Conceptual Framework require that items be measured in a way that satisfies the qualitative characteristics. Application of a one currency unit nominal cost contravenes the qualitative characteristics of relevance, faithful representation, comparability and verifiability. We also note that, conceptually, applying a value of one currency unit is quite different to depreciating an asset to zero.

A nominal cost approach is inconsistent with how we account for other assets that an entity receives in exchange for no consideration, such as donated non-heritage property, plant and equipment. IPSAS 17 requires that where an asset is acquired through a non-exchange transaction, its cost shall be measured at its fair value as at the date of acquisition.

Heritage items are sometimes difficult to value because they are unique, or have no ready market. However, we note that this difficulty is not limited to heritage items; many non-heritage items are also difficult to value.

We consider that when heritage items meet the asset recognition criteria, the measurement requirements at initial recognition should be consistent with the accounting for other assets.

**6. Preliminary View – Chapter 4.1 (following paragraph 4.40)**

Heritage assets should be recognised in the statement of financial position if they meet the recognition criteria in the Conceptual Framework.

Do you agree with the IPSASB's Preliminary View? If not, please provide your reasons.

The NZASB agrees with this Preliminary View.

We encourage the IPSASB to provide additional guidance on how to apply the recognition criteria to heritage items, given their unique characteristics. We note that demonstrating present control, a past event and service potential can be particularly challenging when accounting for heritage items.

We acknowledge that some aspects of Māori heritage may be unique. In particular, the concepts of ownership and asset valuation do not have a parallel in the Māori world-view which makes recognition of Māori heritage problematic for financial accounting purposes. The closest concept to control or ownership of heritage items used by the Māori people is the concept of *Kaitiakitanga* which differs from the legal concept of ownership frequently applied in financial reporting.

*Kaitiakitanga* means guardianship, protection, preservation or sheltering. Traditionally, Māori believe that all life is connected. People are not superior to the natural order; they are part of it. *Kaitiakitanga* grows out of this connection and expresses it in a modern context. *Kaitiakitanga* can apply to valued family items and include family heirlooms such as *korowai* (cloaks), *mere pounamu* (jade clubs) and books about *whakapapa* (genealogy). An item that belongs to a person later becomes the property of all their descendants. It is cared for by an individual *kaitiaki* on behalf of the group. The *kaitiaki* is responsible for bringing the object to important occasions such as funerals, and for holding information about it.

Many Māori heritage items for which the concept of *Kaitiakitanga* applies are on loan to entities such as museums. Māori heritage represents a large proportion of many collections in New Zealand museums. For example, the largest museum in Auckland, New Zealand, has 70% of its Māori collection on loan from the Māori people.

We note that there are many different forms of guardianship of heritage assets such as ownership, co-ownership, lease, loan<sup>4</sup> and hybrid<sup>5</sup> e.g. part-owned and part-leased. An entity would need to consider its rights, and the rights of others, in relation to a heritage item to make a decision about recognition of that item as a heritage asset.

Our constituents would welcome guidance on the accounting for heritage items where the reporting entity has custodian and preservation responsibilities but may not necessarily have "control" or have ownership rights.

<sup>4</sup> Loans maybe for a specific period, or indefinite.

<sup>5</sup> This occurs in Heritage New Zealand's portfolio of Heritage properties.

**7. Specific Matters for Comment – Chapter 4.2 (following paragraph 4.40):**

Are there heritage-related situations (or factors) in which heritage assets should not initially be recognised and/or measured because:

- (a) It is not possible to assign a relevant and verifiable monetary value; or;
- (b) The cost-benefit constraint applies and the costs of doing so would not justify the benefits?

If yes, please describe those heritage-related situations (or factors) and why heritage assets should not be recognised in these situations.

- (a) Assigning a relevant and verifiable monetary value

The NZASB agrees that there are instances where heritage assets are not able to be reliably measured and therefore should not be initially recognised in the statement of financial position. Although non-recognition of heritage assets in such circumstances is appropriate, heritage assets should be recognised when they can be reliably measured.

We encourage the IPSASB to provide guidance on determining what constitutes reliable measurement, reflecting the unique characteristics of heritage assets. Any assistance or pragmatic solutions provided to assist preparers in the determination of the initial measurement of heritage assets will encourage a greater level of reporting of heritage assets in the statement of financial position.

In particular, we consider it important to distinguish measurement of heritage items for financial reporting purposes and measurement for other purposes. In New Zealand there is particular sensitivity surrounding assigning any financial value to cultural assets. Recording individual financial value to *taonga*<sup>6</sup> invites a comparison of value that may be inconsistent or even offensive. Prioritising only “the most valuable” items raises further difficulty, because one significant source of value in a Māori framework is the *mana*<sup>7</sup> of the people connected to the artefact in question. Perception of value can depend on one’s relationship with that person and is something that will alter with context. Items of high value to one *hapu*<sup>8</sup> will not be significant to another so it becomes difficult to establish a hierarchy or any reliable or meaningful relativity.

Therefore, we recommend providing guidance that clarifies the objective of measurement for financial reporting purposes, as distinguished from other purposes.

When a heritage asset cannot be reliably measured, we would encourage the disclosure of information about its nature and significance of any unrecognised heritage assets. In these instances it may be more appropriate to disclose non-financial information about the heritage asset.

- (b) Cost-benefit constraints

Although the Conceptual Framework states that the IPSASB will make assessments about costs and benefits in setting standards,<sup>9</sup> the Conceptual Framework does not suggest that these assessments

<sup>6</sup> *Taonga* means a treasure in Māori culture.

<sup>7</sup> *Mana* means power, prestige or status.

<sup>8</sup> *Hapu* means a number of extended family groups that form a sub-tribe.

<sup>9</sup> Paragraph 3.40 of the *Conceptual Framework for General Purpose Financial Reporting by Public Sector Entities*.



would be made by individual entities. In applying standards, entities need to make judgements about the application of requirements in the standards to individual items, including consideration of materiality. The nature of heritage items is such that the criterion of “reliably measure” needs to be assessed on a case by case basis.

In order for the benefits of information about heritage items to exceed the costs of recognition, in our view, the IPSASB should promote pragmatic approaches to the first-time recognition of heritage items. We acknowledge the difficulty in initial recognition for assets acquired in non-exchange transactions when IPSAS 23 *Revenue from Non-Exchange Transactions* applies. However, we believe that the focus should be on assisting entities to undertake such measurements, rather than non-recognition of heritage items on cost/benefit grounds where a reliable measure can be made. This is because, in our view, the recognition of heritage items is important for accountability purposes.

**8. Preliminary View – Chapter 4.2 (following paragraph 4.40):**

In many cases it will be possible to assign a monetary value to heritage assets. Appropriate measurement bases are historical cost, market value and replacement cost.

Do you agree with the IPSASB’s Preliminary View? If not, please provide your reasons.

We consider that in “some cases” it will be possible to assign a monetary value to heritage assets, but that the assertion that this is possible in “many cases” is overstating the position. The NZASB supports the overall objective of getting more heritage assets onto the balance sheet by helping entities to overcome the difficulties associated with assigning values.

In principle, we consider the initial and subsequent measurement options in IPSAS 17 are appropriate for heritage assets, although we feel additional guidance is needed to apply these approaches to reflect the unique characteristics of heritage assets.

We observe that there is often no market for heritage assets, and entities would find it particularly helpful if additional guidance was provided for determining the market value of heritage assets. There are various bases for arriving at a market value through valuation approaches, including an insurance valuation<sup>10</sup> which may be readily available and relevant. We suggest a wider pragmatic and flexible approach be taken to valuations, including for entities that apply the revaluation model for subsequent measurement, to mitigate the high costs of regular independent valuations (as discussed further in our response to question 10).

We also suggest guidance be provided on what is meant by replacement cost for heritage assets. In some cases, any replacement cost would be for a replica of the asset as the original could not be recreated. For example, in the case of replacement cost of an historic building, is the entity contemplating the replacement of what was already there, or a more modern version more suitable for contemporary needs? Following the 2010/11 Christchurch earthquakes the Christchurch Cathedral was severely damaged. The choice of how to replace Christchurch Cathedral remains with the Christchurch Anglican Diocese which is still undecided as to whether it should rebuild the original (a replica), or build a modern 21<sup>st</sup> Century cathedral<sup>11</sup>.

<sup>10</sup> Although not a market value *per se*, it may be a suitable proxy in the context of a particular valuation.

<sup>11</sup> A third option is to gift the currently damaged ruin “as is” to the people of New Zealand.

**9. Specific Matters for Comment – Chapter 4.3 (following paragraph 4.40)**

What additional guidance should the IPSASB provide through its Public Sector Measurement Project to enable these measurement bases to be applied to heritage assets?

The IPSASB has a range of options available:

- (a) amend standard(s);
- (b) issue new standard(s);
- (c) provide general guidance; or
- (d) facilitate the sharing of specific guidance.

In making this decision, the IPSASB should consider the costs versus the benefits of these options, and the difficulty of being able to address the measurement of the wide range of heritage items such as museum collections, heritage properties and cultural icons.

We consider that the IPSASB issuing general guidance would be the most appropriate outcome. This should encourage more widespread recognition of heritage assets on the balance sheet, which, in turn, should support better management and preservation of heritage assets. Such guidance could draw upon the approaches applied in countries that currently recognise heritage items.

We also recommend that the IPSASB consult the International Valuation Standards Council to ensure that the valuation standards work effectively with the resultant general guidance.

**10. Preliminary View – Chapter 5 (following paragraph 5.14):**

Subsequent measurement of heritage assets:

- (a) Will need to address changes in heritage asset values that arise from subsequent expenditure, consumption, impairment and revaluation.
- (b) Can be approached in broadly the same way as subsequent measurement for other non-heritage assets.

Do you agree with the IPSASB's Preliminary View? If not, please provide your reasons.

We have not identified any reason to disagree with the IPSASB's Preliminary View on the subsequent measurement of heritage assets. In principal, we consider the subsequent measurement options in IPSAS 17 are appropriate for heritage assets. We note that the revaluation approach for subsequent measurement is an accounting policy choice.

However, we would encourage the IPSASB to take a pragmatic approach when developing the subsequent measurement approach requirements and guidance. This could include allowing for greater flexibility by giving consideration to the following.

- (a) Regularity of fair value valuations. Allowing for fair value valuations to be performed, say, once every 10 years, regardless of market movements. In between the periodic valuations, the asset could be considered to be held at cost and be depreciated and impaired accordingly. Requiring valuations to be carried out more regularly may not be relevant, given heritage

assets are expected to be held indefinitely, and are not held for capital appreciation purposes. Our main concern is to ensure that entities are not required to do annual fair value assessments. This suggestion could create a special class of revaluations applicable only to heritage assets.

- (b) Allow rolling valuations over a specified period to spread valuation costs. Some guidance around how to manage this process would be useful for constituents. For example, with a three year valuation period, the guidance should require that only a third of the population need to be fair valued in any year, and the other two-thirds would need no fair value assessment in that year.
- (c) Allow smaller classes of assets based on the assets heritage characteristics and significance (which would particularly assist the art galleries<sup>12</sup>).
- (d) Allow flexibility to change the valuation model on transition to the new accounting requirements for heritage assets. For example, recognise current value as deemed cost on transition.

#### **11. Specific Matter for Comment – Chapter 5 (following paragraph 5.14)**

Are there any types of heritage assets or heritage-related factors that raise special issues for the subsequent measurement of heritage assets?

If so, please identify those types and/or factors, and describe the special issues raised and indicate what guidance IPSASB should provide to address them.

Valuation costs are often identified as an obstacle to the recognition of heritage assets in financial statements. Entities can decide whether or not to revalue a particular class of assets.

For art galleries, a decision to revalue would mean that all art would need to be revalued as the common practice in New Zealand is to treat all art as a single class. Allowing for, say, a triennial rolling valuation would mitigate these costs with all assets having a valuation that is not more than three years old. In contrast, museums tend to hold items across a number of asset classes so the application of the revaluation requirements in standards is not as onerous. Also see our related comments in response to question 10 above.

Due to the nature and age of heritage assets, they often have higher than usual maintenance costs. However, we do not see a pressing need for guidance on how to account for such maintenance costs.

<sup>12</sup> For example, having classes by the century in which a picture was painted, or by artist, instead of having “all paintings” as one class.

**12. Preliminary View – Chapter 6 (following paragraph 6.10)**

The special characteristics of heritage items, including an intention to preserve them for present and future generations, do not, of themselves, result in a present obligation such that an entity has little or no realistic alternative to avoid an outflow of resources. The entity should not therefore recognise a liability.

Do you agree with the IPSASB's Preliminary View? If not, please provide your reasons.

We agree with this Preliminary View, noting that all the facts and circumstances need to be considered.

**13. Preliminary View – Chapter 7 (following paragraph 7.9)**

Information about heritage should be presented in line with existing IPSASB pronouncements.

Do you agree with the IPSASB's Preliminary View? If not, please provide your reasons and describe what further guidance should be provided to address these.

We agree that the current disclosures for accounting for heritage assets are appropriate. Current disclosures are sensible and provide useful information.

Although we support heritage assets that meet the recognition criteria being recognised in financial statements, we acknowledge the limitations of financial statements, and the role that disclosures, or other forms of reporting, have in providing information about heritage items. For example, it is relevant for an entity with responsibility for managing heritage assets to provide information on its management of heritage assets in its service performance report.

As discussed earlier, the NZASB acknowledges that the value obtained for financial reporting purposes is not the only value that a heritage item may have for a community. In particular, the significance of a heritage item to an ethnic group is not readily converted to financial value but is nonetheless an important indicator of heritage in the museum community. The seminal reference on significance is *Significance 2.0, a guide to assessing the significance of collections*, a publication of the Collections Council of Australia Ltd.<sup>13</sup> This guide promotes the writing of a statement of significance for heritage collection items.<sup>14</sup> The statement of significance would usually be a one page summarised pictorial and written statement of the meaning and importance of the specific heritage item. Information from these statements could form the basis for some non-financial disclosures about heritage items.

Some of our constituents were in favour of a separate accounting standard for heritage. Arguments advanced in favour of this option are set out below.

- (a) Signalling to users that heritage was important and had special characteristics.
- (b) Preparers would have a marked delineation for accounting purposes between heritage items and other assets.
- (c) Supporting the request for preservation funding.

<sup>13</sup> <https://www.arts.gov.au/sites/g/files/net1761/f/significance-2.0.pdf>

<sup>14</sup> *Ibid* pp38-41.

- (d) Demonstrating custodial rights and responsibilities.

Although the NZASB considered these arguments in its deliberations, it formed the view that non-mandatory general guidance was its preferred solution. This approach supports the recognition and measurement requirements that already exist in IPSAS 17 and IPSAS 31 for heritage assets that meet the recognition criteria in the IPSASB's Conceptual Framework.

### Informal comments – Respondent 1

The following comments on the IPSASB CP *Financial Reporting for Heritage in the Public Sector* were received by staff via email correspondence dated 23 August 2017.

1. Currently heritage assets (tangible assets) are included in the reporting requirements of IPSAS 17 and (intangible ones) in IPSAS 31. Research shows that heritage assets are of significance in many jurisdictions and have special characteristics that would warrant a separate accounting and reporting standard for such assets. Currently including these assets into Property, Plant and Equipment implies that they are of same nature as other non-current assets and could be treated in a similar but slightly modified way. Providing a one separate standard that would deal with issues around recognition, measurement and disclosure of most if not all heritage assets would not only assist the prepares of the information on heritage assets but it would also signal to the users of such information their importance and their special characteristics.
2. The research on heritage assets has shown (as per papers that I earlier sent you) that heritage items/assets, because of their special characteristics, do require enhanced disclosures. Users are particularly interested in preservation of heritage assets/items for future generations. Therefore, I agree with the points in Chapter 7 of the IPSASB Consultation Paper on Financial Reporting for Heritage in the Public Sector. I do, however, suggest that point 7.8 is to say 'should' rather than 'could' when it comes to entities presenting information in their financial statements.

### Informal comments – Respondent 2

The following comments on our draft Comment Letter on the IPSASB CP *Financial Reporting for Heritage in the Public Sector* were received by staff via email correspondence dated 31 August 2017.

In general I agree with your comments, although I do feel that there is still more that could be done to ease and clarify the expectations for museum and gallery collections – but probably without making any change to the actual regulations. I have a few notes, comments and questions.

Comments on your drafts

- In general it seems to me to be a fair reporting of our views
- I think it noteworthy that there are significant variations between the practices and perspectives of the museums consulted – and their auditors. e.g, some auditors give qualified opinions while others accept non-disclosure on the basis that the value ‘cannot be reliably measured’.
- I agree re the inadvisability of the proposed nominal 1 CU valuation.



NZ ACCOUNTING  
STANDARDS  
BOARD

## Memorandum

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**Date:** 1 September 2017

**To:** NZASB Members

**From:** Aimy Luu Huynh and Anthony Heffernan

**Subject:** **IPSASB Consultation Paper *Accounting for Revenue and Non-Exchange Expenses***

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### Action required<sup>1</sup>

1. The Board is asked to:
  - (a) NOTE the IPSASB Consultation Paper *Accounting for Revenue and Non-Exchange Expenses* (the CP);
  - (b) AGREE the proposed project plan and outreach for the CP; and
  - (c) AGREE the areas of focus for the CP.

### Background

2. The IPSASB published the Consultation Paper *Accounting for Revenue and Non-Exchange Expenses* (CP) in August. Comments are due to the NZASB by 22 November 2017 and to the IPSASB by 15 January 2018.
3. The Board wrote to the IPSASB staff encouraging them to reconsider extending the comment period to six months. The IPSASB staff considered our letter and at the time of their reply the comment period for the CP was kept at four months. Our letter and the IPSASB staff's response are agenda items 2.3.2 and 2.3.3 respectively. Subsequent to the IPSASB staff's response, the CP was issued with a five-month comment period. The extension to a five-month comment period does not alleviate the time pressure on the development of our comment letter: the additional comment period is over the Christmas/New Year period.
4. The IPSASB initiated the project to address:
  - (a) the challenges experienced by preparers of financial statements when determining whether revenue transactions are exchange or non-exchange and the value of this distinction for users of the financial statements;

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<sup>1</sup> This memo refers to the work of the International Accounting Standards Board (IASB) and uses registered trademarks of the IFRS Foundation (for example, IFRS® Standards, IFRIC® Interpretations and IASB® papers).



- (b) the gap in the current IPSASB literature on non-exchange expenses, which may lead to ambiguity and inconsistency of accounting policies in a highly significant area of expenditure;
  - (c) application issues with IPSAS 23 *Revenue from Non-Exchange Transactions (Taxes and Transfers)* — the primary concern being that IPSAS 23 is too restrictive in not allowing revenue to be recognised over time when funding is received for a specific purpose, but there are no return obligations; and
  - (d) convergence with IASB literature, which has diminished with the publication of IFRS 15 *Revenue from Contracts with Customers*.
5. At the August meeting, the Board agreed to provide comments on the CP. The Board also agreed to reconvene the Working Group that was set up when the CP was being drafted.

### Structure of this memo

6. The remaining sections of this memo are:
- (a) the proposed project plan;
  - (b) the proposed outreach;
  - (c) an overview of the CP and the recommended areas of focus for the comment letter; and
  - (d) next steps.

### Proposed project plan

7. The appendix to this memo contains the proposed project plan, showing the dates for the Board and Working Group meetings and outreach.
8. The Working Group has representatives from the public sector and not-for-profit (NFP) sector. This group will assist the Board in forming its comments on the CP.
9. The broad approach of the project plan is to discuss the CP proposals with the Working Group and then to discuss the CP proposals, along with the Working Group's comments, with the Board. We are proposing separate discussions for the Working Group and Board in the following order.
- (a) Revenue recognition approaches.
  - (b) Non-exchange expense recognition approaches.
  - (c) Draft comment letter.
10. Throughout the comment period we will complete constituent outreach activities to support the development of our comment letter, and to support the deliberations of both the Working Group and Board.

11. The project plan proposes an additional Board meeting on 6 October and we may also need an additional Board meeting in early November. The additional November meeting is subject to sufficient time being allocated to this project at the November NZASB meeting.
12. We will likely require a sub-committee (after the December NZASB meeting) to complete a final review and approval of the comment letter before it is submitted in January 2018.

#### **Proposed outreach**

13. This is an important topic that affects most public benefit entities (PBEs) in both the public sector and NFP sector. We would like to inform as many constituents as possible that the CP has been issued and encourage the submission of comments to us or directly to the IPSASB.
14. Our proposals for outreach activities are to:
  - (a) hold a webinar. The aim is to increase awareness of the CP and discuss the key proposals contained in the CP (focusing on the different revenue and non-exchange expense recognition approaches);
  - (b) present at the CA ANZ NFP special interest groups (SIG) if this fits in with their schedules. At this stage the NFP SIG presentation in Wellington has been confirmed;
  - (c) seek feedback from External Reporting Advisory Panel (XRAP) and our Technical Reference Group (TRG); and
  - (d) promote the webinar and CP through Charities Services' communication channels such as their newsletter.
15. To promote awareness of the CP, we also plan to provide links on the XRB website to relevant IPSASB materials, such as webinar, At a Glance publications etc.

#### **Overview of the CP**

16. PBEs often enter into transactions that require determining the appropriate accounting period for revenue and non-exchange expenses recognition—especially for funding arrangements that cover multiple accounting periods. A key objective of this CP is to seek views on potential recognition and measurement approaches for these often-significant transactions.
17. The CP is over 80 pages long containing seven chapters and two appendices. The CP has nine preliminary views and seven specific matters for comment.
18. Table 1 provides an overview of the CP and staff's recommendation on the topics our comment letter should focus on. The short comment period limits our ability to provide detailed comments on everything in the CP so we recommend focusing on the key issues. Table 1 does not provide a summary of Chapter 1 Introduction and Chapter 2 Current Revenue Recognition Standards as these chapters provide background to the CP.
19. If the Board agrees with the recommended key issues, we will provide further analysis of these topics at future board meetings.

Table 1

Topic	Key points in CP	Key issue Type of comments
Chapter 3 Analysing public sector transactions with reference to performance obligations	<p>The IPSASB has grouped public sector revenue and non-exchange expense transactions into three broad categories in order to explore the approaches in the CP.</p> <ul style="list-style-type: none"> <li>• Category A: Revenue and non-exchange expense transactions with no performance obligations or stipulations.</li> <li>• Category B: Revenue and non-exchange expense transactions that contain performance obligations or stipulations, but do not have all the characteristics of a transaction within the scope of IFRS 15.</li> <li>• Category C: Revenue transactions that are within the scope of IFRS 15. This category includes transactions involving the transfer of promised goods or services to customers as defined in IFRS 15.</li> </ul> <p>The IPSASB has an objective of convergence with IFRS Standards where appropriate. Therefore, for public sector revenue transactions which are similar in nature and substance to for-profit revenue transactions, standards-level requirements and guidance of the IPSASB and IASB should be converged and provide the same outcome. Therefore the IPSASB considers that it is appropriate to replace IPSAS 9 <i>Revenue from Exchange Transactions</i> and IPSAS 11 <i>Construction Contracts</i> (Category C transactions) with an IPSAS primarily based on IFRS 15.</p> <p>The extent of the modifications for an IPSAS converged with IFRS 15 will generally be limited to terminology rather than substance.</p> <p>Category A transactions do not contain performance obligations or stipulations. The guidance will be provided in an updated IPSAS 23.</p>	<p>No. This will not be a key area of focus.</p> <p>The IPSASB's categorisation of transactions is used as a way to explore the approaches proposed by the CP.</p> <p>The proposed output for Category A and Category C transactions seems appropriate.</p> <p>We recommend our comment letter provide <i>high level comments</i> on this chapter. We will focus our attention on the proposals for the wide range of Category B transactions (chapter 4).</p>
Chapter 4 Revenue Transactions (Category B) – recognition approaches	<p>The CP evaluates two approaches for dealing with Category B revenue transactions.</p> <ul style="list-style-type: none"> <li>• Approach 1 The Exchange/Non-Exchange Approach – Update to IPSAS 23: the current distinction between exchange and non-exchange transactions is retained as the primary</li> </ul>	<p>Yes. This will be a key area for seeking comments and views from the Working Group, Board and</p>

Topic	Key points in CP	Key issue Type of comments
	<p>determinant of accounting treatments for both Category A and Category B transactions. Within this approach, five options are considered to address some of the issues with IPSAS 23 (see below).</p> <ul style="list-style-type: none"> <li>• Approach 2 The Public Sector Performance Obligation Approach (PSPOA): this approach is the modified form of the IFRS 15 five-step approach, which reflects the public sector context. Further details of this approach are provided below.</li> </ul> <p><u>Approach 1 The Exchange/Non-Exchange Approach – Update to IPSAS 23</u></p> <ul style="list-style-type: none"> <li>• Option (a) – Provide additional guidance on making the exchange/non-exchange distinction This option does not address the timing issue of revenue recognition so this option could be used in combination with the four options below.</li> <li>• Option (b) – Require enhanced display/presentation for transactions with time requirements Using presentation to indicate the resource provider's intention as to how the transfer is used. This may be through note disclosures that, for example, within accumulated surplus/deficit is a resource that will be used by the resource recipient in one or more future reporting periods. An alternative or supplement to this disclosure is disaggregation of revenue in the statement of financial performance and net assets/equity identifying resources that will be used by the resource recipient in one or more future reporting periods.</li> <li>• Option (c) – Classify time requirements as a condition This option would give rise to a liability until the resources are used as intended. This option would involve modifying the definition of a condition on a transferred asset to specifically include time requirements. The IPSASB has strong reservations about this approach because the "liability" has no return obligation and is</li> </ul>	<p>constituents through outreach activities.</p> <p>We will consider whether the proposed approaches are appropriate for the wide range of Category B transactions and if they will resolve current revenue recognition concerns raised by constituents.</p> <p>We recommend our comment letter provide <i>detailed comments</i> on this chapter.</p>

Topic	Key points in CP	Key issue Type of comments
	<p>unlikely to meet the definition of a liability in the IPSASB Conceptual Framework.</p> <ul style="list-style-type: none"> <li>Option (d) – Classify transfers with time requirements as other obligations This approach accepts these transfers do not give rise to a liability but it is in the public interest for the recipient to recognise an “other obligation” on the balance sheet. This would convey to users of the financial statements that the recipient has resources intended for use in subsequent reporting periods.</li> <li>Option (e) – Recognise transfers with time requirements in net assets/equity and recycle through statement of financial performance. This approach may implicitly introduce “other comprehensive income” into the IPSASB literature without exploring the conceptual basis for doing so.</li> </ul> <p><u>Approach 2 The PSPOA</u></p> <p>This approach focuses on arrangements that have performance obligations. The five steps are:</p> <ul style="list-style-type: none"> <li>Step 1 – Identify the binding arrangement In the public sector many arrangements for the provision of resources are non-contractual so it is appropriate to relabel contracts with binding arrangements. In the public sector the interpretation of enforceability would need to go beyond an obligation of the resource recipient to return resources directly to the resource provider to remedies in the event of non-fulfilment of a performance obligation.</li> <li>Step 2 – Identify the performance obligations The services to be provided under the arrangement have to be specified or distinct so that performance obligations can be identified.</li> <li>Step 3 – Determine the consideration In the arrangement, there has to be some linkage between the amount of agreed consideration and the fulfilment of performance obligations.</li> <li>Step 4 – Allocate the consideration The IPSASB considers it would be appropriate to place less emphasis on the need to determine</li> </ul>	

Topic	Key points in CP	Key issue Type of comments
	<p>the “stand-alone selling price” and instead focus on an entity’s ability to determine cost of fulfilling each performance obligation as a basis for allocating the total amount of agreed consideration to each performance obligation.</p> <ul style="list-style-type: none"> <li>Step 5 – Recognise revenue</li> </ul> <p>The recognition of revenue as performance obligations are fulfilled relies on the ability of the resource recipient to determine that a performance obligation has been fulfilled or is in the process of being fulfilled.</p> <p>The IPSASB considers that Category B transactions should be accounted for using the PSPOA.</p>	
Chapter 5 Current IPSAS 23 issues – capital grants	<p>The CP acknowledges the main concern with capital grants is the pattern of revenue recognition.</p> <p>The CP has not provided any proposals for the accounting for capital grants. Instead the CP is gathering issues and possible solutions from respondents.</p>	<p><i>No.</i> This will not be a key area of focus.</p> <p>The CP is gathering issues and possible solutions. We will have the opportunity to provide comments when the IPSASB has made further progress on this topic.</p> <p>We recommend our comment letter provide <i>high level comments</i> on this chapter, emphasising the accounting for capital grants is an issue for our constituents and to encourage the IPSASB to develop appropriate solutions.</p>
Chapter 5 Current IPSAS 23 issues – services in-kind	<p>The main concerns with services in-kind is whether it is an asset and, if so, obtaining a reliable measurement.</p> <p>The following approaches for the accounting of services in-kind are discussed.</p> <ul style="list-style-type: none"> <li>Require services in-kind to be recognised as an asset when the fair value can be measured reliably and the services would have been purchased if not donated.</li> <li>Allow services in-kind to be recognised if the fair value can be measured reliably regardless of</li> </ul>	<p><i>No.</i> This will not be a key area of focus.</p> <p>The current guidance in IPSAS 23 acknowledges the concerns with services in-kind and permits but does not require the recognition.</p> <p>We recommend our comment letter provide <i>high level comments</i> on this chapter.</p>

Topic	Key points in CP	Key issue Type of comments
	<p>whether the services would have been purchased if not donated.</p> <ul style="list-style-type: none"> <li>Require services in-kind to be recognised if significant in the context of an entity's overall activities.</li> </ul>	
Chapter 6 Non-exchange expenses – recognition approaches	<p>The CP addresses the following types of non-exchange expenses.</p> <ul style="list-style-type: none"> <li>Universally accessible services.</li> <li>Collective goods and services.</li> <li>Grants, contributions and other transfers.</li> </ul> <p>The proposed scope for the Social Benefits project are benefits provided to mitigate social risks, which are principally state pensions, unemployment benefits and income support.</p> <p>The CP explores two approaches for the initial recognition of non-exchange expenses.</p> <ul style="list-style-type: none"> <li>The Extended Obligating Event Approach: the determining factor of whether a resource provider has a liability and expense or asset is whether there is an obligating event. For transactions that include stipulations on the resource recipient, a mirrored approach to IPSAS 23 would be used to determine whether expenses related to that liability are recognised immediately or over time.</li> <li>The PSPOA: this approach is the counterpart to the approach for revenue transactions, see above. The five-step approach has been reconfigured from the perspective of the resource provider. The essence of this approach is the resource provider recognising an expense when the resource recipient satisfies identified performance obligations.</li> </ul> <p>The IPSASB's preliminary views are:</p> <ul style="list-style-type: none"> <li>universally accessible services and collective goods and services impose no performance obligations on the resource recipient and there is no obligating event related to the transactions. These transactions should be recognised as an expense as services are delivered; and</li> <li>where grants, contributions and other transfers contain either performance obligations or</li> </ul>	<p>Yes. This will be a key area for seeking comments and views from the Working Group, Board and constituents through outreach activities.</p> <p>The gap in IPSAS literature on non-exchange expenses has led to diversity in practice.</p> <p>We recommend our comment letter provide <i>detailed comments</i> on this chapter.</p>

Topic	Key points in CP	Key issue Type of comments
	stipulations, these should be accounted for using the PSPOA.	
Chapter 7 Measurement of non-contractual receivables and non-contractual payables	<p>The IPSASB's preliminary views are:</p> <ul style="list-style-type: none"> <li>at initial recognition, non-contractual receivables should be measured at face value (legislated amount) of the transaction(s) with any amount expected to be uncollectible identified and impaired. This approach promotes accountability and is in the public interest; and</li> <li>the subsequent measurement of non-contractual receivables should use the fair value approach.</li> </ul> <p>For non-contractual payables, four approaches for subsequent measurement are discussed. The approaches are:</p> <ul style="list-style-type: none"> <li>Approach 1 – Cost of fulfilment</li> <li>Approach 2 – Amortised cost</li> <li>Approach 3 – Hybrid (of approach 1 and 2)</li> <li>Approach 4 – IPSAS 19 <i>Provisions, Contingent Liabilities and Contingent Assets</i> requirements</li> </ul>	<p><i>No.</i> This will not be a key area of focus.</p> <p>Whilst there is a lack of guidance in the IPSAS literature for the measurement of non-contractual receivables and non-contractual payables, preparers have developed appropriate accounting policies from the current IPSAS literature.</p> <p>We recommend our comment letter provide <i>high level comments</i> on this chapter.</p>

### Next steps

20. Following feedback from the Working Group's first meeting, staff will prepare an issues paper on chapter 4 of the CP. This paper will be for the additional Board meeting on 6 October.

### Recommendations

21. We recommend that the Board:
- (a) AGREES the project plan for the CP;
  - (b) AGREES the proposed outreach for the CP; and
  - (c) AGREES the areas of focus for the CP.

### Attachments

Agenda item 9.2: IPSASB Consultation Paper *Accounting for Revenue and Non-Exchange Expenses*

Agenda item 9.3: IPSASB At a Glance: *Accounting for Revenue and Non-Exchange Expenses*



## Appendix: Project Plan

	Aug	Sep	Oct	Nov	Dec
<b>Comment letter development plan</b>					
Working Group meetings		15 Sep Discussion of Issues – Revenue	13 Oct Discussion of Issues – Non-exchange expenses and other issues	21 Nov Review of draft comment letter	
NZASB meetings	2 Aug NZASB agreed to comment	13 Sep Project and outreach plan Areas of focus	6 Oct 9am–12pm (additional) Discussion of Issues – Revenue	1 Nov Discussion of Issues – Non-exchange expenses and other issues	14 Dec Review of draft comment letter
NZASB sub-committee					20 Dec Review and approve updated comment letter
<b>Outreach plan</b>					
InterChurch Bureau meeting	23 Aug Awareness of CP Discussion on NFP issues				
Webinar		28 Sep CP awareness			
XRAP		12 Sep Discussion of grant revenue issues			
TRG		15 Sep Discussion of grant revenue issues			
CA ANZ SIG <sup>2</sup>			17 Oct NFP (Wgtn) Awareness of CP Gather NFP issues		

<sup>2</sup> We have also contacted the Auckland NFP SIG and Christchurch NFP SIG. Attendance at these meetings is to be confirmed.



**EXTERNAL REPORTING BOARD**  
*Te Kāwai Ārahi Pūrongo Mōwaho*

## **APPROVAL NZASB 89**

### **Approval to Issue NZ IFRIC 23 *Uncertainty over Income Tax Treatments***

In accordance with the protocols established between the New Zealand Accounting Standards Board (NZASB) and the External Reporting Board (XRB Board), the NZASB has:

- approved for issue NZ IFRIC 23 *Uncertainty over Income Tax Treatments*; and
- provided a signing memo outlining the due process followed before reaching that decision, and other related information.

I have reviewed the signing memo and am satisfied with the information provided. Accordingly, the NZASB is hereby authorised to issue NZ IFRIC 23 *Uncertainty over Income Tax Treatments* pursuant to section 12(a) of the Financial Reporting Act 2013.

Dated this 7<sup>th</sup> day of August 2017

A handwritten signature in blue ink, reading 'Graeme R Mitchell', is written over a dotted line.

Graeme R Mitchell  
Chairman  
External Reporting Board



**EXTERNAL REPORTING BOARD**

*Te Kāwai Ārahi Pūrongo Mōwaho*

## **APPROVAL NZASB 90**

### **Approval to Issue NZ IFRS 17 *Insurance Contracts***

In accordance with the protocols established between the New Zealand Accounting Standards Board (NZASB) and the External Reporting Board (XRB Board), the NZASB has:

- approved for issue NZ IFRS 17 *Insurance Contracts*; and
- provided a signing memo outlining the due process followed before reaching that decision, and other related information.

I have reviewed the signing memo and am satisfied with the information provided. Accordingly, the NZASB is hereby authorised to issue NZ IFRS 17 *Insurance Contracts* pursuant to section 12(a) of the Financial Reporting Act 2013.

Dated this <sup>7<sup>th</sup></sup>.....day of August 2017

A handwritten signature in blue ink, reading 'Graeme R Mitchell', written over a dotted line.

Graeme R Mitchell  
Chairman  
External Reporting Board