



International Public Sector Accounting Standard 35
Consolidated Financial Statements

IPSASB Basis for Conclusions – as per 2017 IPSASB Handbook

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Basis for Conclusions

This Basis for Conclusions accompanies, but is not part of, IPSAS 35.

Objective

- BC1. This Basis for Conclusions summarizes the IPSASB's considerations in reaching the conclusions in IPSAS 35. As this Standard is based on IFRS 10, *Consolidated Financial Statements* (issued in 2011, including amendments up to December 31, 2014) issued by the IASB, the Basis for Conclusions outlines only those areas where IPSAS 35 departs from the main requirements of IFRS 10, or where the IPSASB considered such departures.

Overview

- BC2. In 2012 the IPSASB commenced work on a project to update those IPSASs that dealt with accounting for interests in controlled entities, associates and joint ventures. In October 2013 the IPSASB issued Exposure Drafts (EDs) 48 to 52 which were collectively referred to as *Interests in Other Entities*. ED 49 *Consolidated Financial Statements* was based on IFRS 10 *Consolidated Financial Statements*, having regard to the relevant public sector modifications in IPSAS 6, *Consolidated and Separate Financial Statements*. In January 2015 the IPSASB issued five new IPSASs, including IPSAS 35. These new IPSASs supersede IPSAS 6, IPSAS 7, *Investments in Associates* and IPSAS 8, *Interests in Joint Ventures*.

Process

- BC3. In developing the Standard the IPSASB had regard to those aspects of IPSAS 6 that had been developed specially to address public sector issues or circumstances that are more prevalent in the public sector than in other sectors. The IPSASB focused on addressing these issues in the Standard. The IPSASB also had regard to the guidance on assessing whether an entity is controlled for the purposes of the *Government Finance Statistics Manual 2014* (GFSM 2014) with the aim of avoiding unnecessary differences. In developing additional examples that illustrated the public sector environment the IPSASB also considered guidance developed by national standard setters or by bodies with oversight responsibilities for sectors of government.

Alignment with Government Finance Statistics

- BC4. Both at the time of developing ED 49, and as part of the process of finalizing the Standard, the IPSASB considered an analysis of similarities and differences between the definition of control, together with the associated indicators and guidance in GFSM 2014 (and the 2008 System of National Accounts (2008 SNA) with which the GFSM 2014 is harmonized) and the proposed Standard. The IPSASB noted that some of the differences between GFSM and financial reporting are due to their nature and differing objectives. For example, the classification of institutional units into sectors based on their economic nature of being government units will continue to be a significant difference between macroeconomic statistical reporting and accounting and financial reporting. Furthermore, the distinction between market producers and nonmarket producers in macroeconomic statistics would continue to result in a difference in terms of classification to either the general government sector or the public corporations sector, and therefore the overall classification to the public sector, even if there was exactly the same principle and conceptual guidance on the notion of control.
- BC5. During the development of the Standard the IPSASB made a number of efforts to align more closely with guidance in GFSM 2014 or to explain more clearly the nature of differences. Issues in respect of which the IPSASB specifically considered GFSM requirements included:
- (a) Whether to require the consolidation of all controlled entities, as opposed to reporting by sectors of government;
 - (b) The similarity between the concept of control in the Standard and the approach taken in GFSM 2014, including consideration of the indicators of control of nonprofit institutions and corporations in 2008 SNA;

- (c) The differences between regulatory control and control for financial reporting purposes; and;
- (d) The rights associated with golden shares.

Some of these matters are discussed in more detail in later sections of this Basis for Conclusions.

Scope (paragraphs 3–11)

Wholly-Owned and Partly-Owned Controlling Entities

- BC6. The IPSASB agreed that, consistent with the requirements in IPSAS 6 and IFRS 10, wholly-owned or partly-owned controlling entities that meet certain conditions, and post-employment or other long-term employee benefit plans should not be required to present consolidated financial statements. The IPSASB decided that a controlling entity which itself is a controlled entity should not be required to present consolidated financial statements only if “users of such financial statements are unlikely to exist or their information needs are met by the controlling entity’s consolidated financial statements”. This limitation is intended to protect users where such controlling entities represent key sectors or activities of a government and there are users that need consolidated financial statements for accountability or decision making purposes.

Application of the Consolidation Requirements to all Controlled Entities

- BC7. The IPSASB noted the general principle in both IFRS 10 and IPSAS 6 that a controlling entity should consolidate, on a line by line basis, all of its controlled entities. The IPSASB noted that over recent years the potential scale and complexity of a public sector entity’s involvement with other entities (particularly the relationships between a government and other entities) had increased. Government interventions had been a contributing factor to governments (and other public sector entities) having a broad range of interests in other entities, some of which could give rise to control as defined in this Standard. The implications of consolidation when a government has a large number of controlled entities, controlled entities carrying out activities that were formerly regarded as solely private sector activities, and controlled entities where control is intended to be temporary, had led some to query whether consolidation of all controlled entities was justified, having regard to the costs and benefits of doing so.
- BC8. The IPSASB deliberated extensively on the issue of whether all controlled entities should be consolidated, having regard to users’ needs. The IPSASB focused on the information provided by consolidated financial statements, whilst noting that users’ information needs may also be met through other statements and reports such as (i) separate financial statements of both controlling and controlled entities; (ii) performance reports; and (iii) statistical reports. Although some of the IPSASB’s discussions were relevant to any type of public sector entity that is a controlling entity, many of the matters considered were more pertinent at the whole of government level. The IPSASB considered views on the usefulness of consolidation in relation to the following types of controlled entities (whilst noting that these broad categories would not be universally applicable):
- (a) Departments and ministries;
 - (b) Government agencies;
 - (c) [Government Business Enterprises (GBE)] (the term in square brackets is no longer used following the issue of *The Applicability of IPSASs* in April 2016);
 - (d) Financial institutions (excluding government sponsored enterprises); and
 - (e) Other investments (including intentional investments, incidental investments and investment entities). The term “incidental investments” was used to refer to interests acquired in the course of meeting another objective, such as preventing the collapse of a private sector entity.
- BC9. The IPSASB noted that, although there was general agreement that consolidation of controlled departments and ministries and government agencies is appropriate, some members were less certain that the cost of preparing consolidated financial information was justified for other categories of controlled entities.
- BC10. The IPSASB noted arguments in support of requiring consolidation of all controlled entities of a government, including the following:

- (a) Consolidated financial statements provide a panoramic view of a government's activities and current financial position. This panoramic view ensures that users do not lose sight of the risks associated with certain sectors. It shows the performance of the government as a whole.
 - (b) Identifying categories of entities which should not be consolidated could be difficult. Such attempts could lead to rules-based standards. For example, there could be difficulties in separately identifying entities rescued from financial distress on a consistent basis across jurisdictions and over time. Similar issues could arise in respect of any separate proposals for GBEs. Although the term GBE was a defined term within IPSASs when this Standard was issued, the IPSASB noted that there were differences in the way this definition is being applied in practice in different jurisdictions. In addition to the issue of clearly identifying any group of entities for which different accounting requirements would be appropriate, the IPSASB noted that similar activities can be conducted by a variety of entity types both within and across jurisdictions. So, although proposals for different accounting treatments might lead to consistent treatment for a group of entities within a jurisdiction, it might not result in comparable accounting for similar activities.
 - (c) Consolidation of all controlled entities is an example of like items being accounted for in like ways. Exceptions to consolidation reduce the coherence of the financial statements. Given that there could be a number of entities that could potentially be regarded as warranting separate treatment or disclosure, this could adversely affect the coherence of consolidated financial statements.
 - (d) Whole of government financial statements have a different perspective from separate financial statements. Separate financial statements provide information on the activities of the core government.
- BC11. The IPSASB also noted arguments that have been raised in opposition to consolidation of certain controlled entities of a government, including the following:
- (a) The consolidation of entities that have activities that differ from the activities of the core government could obscure the presentation of the results and the condition of the government itself. This argument was raised in relation to a variety of controlled entities including manufacturing activities, large financial institutions, temporarily controlled entities and entities with financial objectives as opposed to social objectives.
 - (b) Some consider that equity accounting for certain categories of controlled entities provides appropriate information on financial performance subsequent to acquisition without incurring high costs or obscuring information about the core government.
 - (c) Some consider that it is inappropriate to consolidate entities that have been rescued from financial distress because they do not represent core government activities and are not intended to be long-term investments.
 - (d) Where governments have high numbers of controlled entities the costs of the consolidation process are high and may be perceived to outweigh the benefits of consolidating those entities on a line by line basis.
- BC12. Reflecting on these arguments for and against requiring consolidation of all controlled entities the IPSASB had regard to:
- (a) The objectives of financial reporting, as outlined in *The Conceptual Framework for General Purpose Financial Reporting by Public Sector Entities (Conceptual Framework)*;
 - (b) The limited availability of evidence on user needs and usefulness of consolidated financial information (particularly on the usefulness of consolidated financial information in respect of specific types of controlled entities);
 - (c) The context within which whole of government consolidated financial statements are prepared;
 - (d) The interaction between the definition of control and the consolidation requirements in the proposed Standard; and
 - (e) The IPSASB's role as an international accounting standard setter.
- BC13. With regard to the objectives of financial reporting, the IPSASB noted that Chapter 2 of the *Conceptual Framework* identifies the objectives of financial reporting as being to provide information that is useful

for accountability purposes and for decision-making purposes. Because of the importance of the budget in the public sector (and the importance of demonstrating compliance with the budget) the IPSASB considered an argument that consolidated financial statements should consolidate only those entities that comprise a government's budget entity. However, the IPSASB agreed that a budget entity approach would not be appropriate for general purpose financial reporting because:

- (a) Decisions about which entities are included in a government's budget may be based on factors other than the degree of autonomy of the entity and the extent to which it provides market goods or makes a commercial return.
- (b) Decisions about which entities are included in a government's budget are often related to whether the entity's activity is intended to be self-funding. The exclusion of self-funding entities from a government's budget, essentially allows the offsetting of revenue and expenses for those activities and means that budget sector information does not reflect the substance of all transactions controlled by a government.
- (c) The budget boundary for a jurisdiction is determined within a jurisdiction. If financial reporting were based on budget sectors there would not be standardized and comparable financial reporting by governments in an international context.

BC14. IPSAS 6 required the consolidation of all controlled entities apart from controlled entities where there was evidence that (a) control was intended to be temporary because the controlled entity was held exclusively with a view to its disposal within twelve months from acquisition and (b) management was actively seeking a buyer. Such temporarily controlled entities were required to be accounted for as financial instruments. The IPSASB considered whether this treatment of temporarily controlled entities should also be required in the proposed Standard. The IPSASB noted a number of concerns regarding the requirements in IPSAS 6. These included:

- (a) The difficulty of identifying temporarily controlled entities;
- (b) The difficulty of justifying a different accounting treatment for controlled entities that are held for more than a couple of years (which can occur with some entities that are initially considered to be temporarily controlled);
- (c) The difficulty of disposing of an investment in its current form. A public sector entity may need to retain responsibility for certain risks in order to dispose of its investment in a temporarily controlled entity. Accounting for such entities as financial instruments provides only a partial representation of the risks associated with the investment;
- (d) If a public sector entity is exposed to risks from an investment in a "temporarily" controlled entity, these risks should be reported consistently with the risk exposures from other controlled entities; and
- (e) The provision of additional explanations by the reporting entity can address some of the issues that arise when large temporarily controlled entities are consolidated.

BC15. The IPSASB therefore decided not to require a different accounting treatment for temporarily controlled entities. Respondents to ED 49 generally agreed with this proposal, for similar reasons to the IPSASB. In discussing respondents' comments the IPSASB acknowledged the arguments made by those that considered there should be an exemption from consolidation for temporarily controlled entities, particularly those acquired by a government to protect the interests of citizens. However, the IPSASB also noted the experience of various jurisdictions in accounting for such situations and that consolidation of such entities had occurred in some jurisdictions. The IPSASB also considered the weight of the support for the removal of the exemption. Respondents noted that such investments can ultimately be held for longer periods than originally envisaged. Some respondents encouraged the IPSASB to consider requiring additional disclosures in respect of entities acquired with a view to disposal. The IPSASB agreed to require disclosure of interests in other entities held for sale in IPSAS 38, *Disclosure of Interests in Other Entities*.

BC16. In considering the existence of research regarding the usefulness of consolidated financial statements in meeting user needs, the IPSASB noted that although an increasing number of governments are applying the accrual basis of accounting, this has been a relatively recent trend and consolidation is often implemented in stages, with core government activities being consolidated first, followed by the

consolidation of other categories of entities as time and resources permit. As a result, there are few jurisdictions that currently present consolidated whole of government financial statements, and empirical research on the usefulness of consolidated whole of government financial statements has been limited. Research to date has tended to focus on who uses consolidated financial statements and the overall benefits of consolidated financial statements, as opposed to the usefulness of consolidating certain types of controlled entities or accounting for them in an alternative way. As part of its deliberations the IPSASB did consider alternative ways of accounting for and presenting information on subsets of controlled entities such as temporarily controlled entities. The IPSASB noted the difficulties of consistently identifying categories of controlled entities that might be accounted for differently or subject to additional disclosures.

- BC17. The IPSASB noted that in developing its requirements for investment entities the IASB focused on user needs. Matters considered by the IPSASB in relation to investment entities are discussed later in this Basis for Conclusions.
- BC18. The IPSASB noted that many governments prepared statistical reports which present consolidated financial information in a sectoral approach, breaking down between the general government sectors and public corporation sectors (Non-Financial and Financial). This information is compiled in accordance with statistical guidance in the 2008 SNA, which, in turn, is consistent with guidance in the GFSM 2014 and the European System of Accounts (ESA 2010). The IPSASB considered whether such a statistical approach could be considered as an alternative to the compilation of whole of government accounts based on the IPSAS approach. The IPSASB noted that IPSAS 22, *Disclosure of Financial Information about the General Government Sector* provides guidance on the presentation of such statistical information in consolidated financial statements. However, IPSAS 22 neither requires the provision of such information in consolidated financial statements, nor permits the presentation of such information as an alternative to consolidation of all controlled entities. Although the IPSASB noted that statistical reporting serves an important role and provides information that is comparable across countries, the IPSASB agreed that such information had a different objective and did not fulfill the role of consolidated financial statements in giving an overview of all government activity. The IPSASB also noted that mandating the provision of statistical sector information by governments other than national governments could be difficult. The IPSASB therefore agreed that any changes to IPSAS 22 should not form part of its project to update IPSASs 6 to 8. Although the IPSASB decided not to provide guidance in this Standard on the presentation of information on statistical sectors, it noted that governments may present consolidated financial statements that are disaggregated by statistical sector.
- BC19. ED 49 therefore proposed the consolidation of all controlled entities, other than the exception(s) from consolidation relating to investment entities (discussed separately in this Basis for Conclusions). The IPSASB sought the views of constituents as to whether there are any categories of entities that should not be consolidated, with any proposals for non-consolidation being justified having regard to user needs. Respondents were generally supportive of this proposal, although a number of respondents highlighted implementation difficulties (for example, the costs associated with consolidating a large number of controlled entities). Some respondents also commented on the existence of reporting entities established through legal or administrative means and noted that they may differ from the reporting entity identified in accordance with the proposed Standard. The IPSASB agreed to acknowledge, in the Standard, the existence of reporting entities established through legal or administrative means.

Investment Entities

- BC20. In October 2012 the IASB issued *Investment Entities* (Amendments to IFRS 10, IFRS 12 and IAS 27). As a result of these amendments IFRS 10 requires that a controlling entity that is an investment entity account for most of its investments at fair value through profit or loss, as opposed to consolidating them. The IPSASB considered the appropriateness of the requirements in IFRS 10 for similar entities in the public sector. The IPSASB first considered which entities might be affected by such requirements. Entities that might meet the definition of an investment entity include some sovereign wealth funds, some pension funds and some funds holding controlling interests in public-private partnership projects (PPP) or private finance initiatives (PFI). The IPSASB noted that any requirements applicable only to investment entities might apply to a relatively small number of public sector entities (having regard to the types of entities that might be investment entities and the fact that these entities might be required to report in accordance with a range of accounting standards, including domestic standards).

- BC21. The IPSASB noted the comments made by respondents to the IASB in relation to the IASB's investment entity proposals and considered that similar arguments would apply in the public sector. Indeed, the IPSASB noted that some types of entities specifically identified by the IASB as potential investment entities (for example, sovereign wealth funds) could be public sector entities applying IPSASs. The IPSASB noted the IASB's focus on user needs in the IASB's deliberations on investment entities. The IPSASB noted that, depending on the reporting framework of the jurisdiction in which they operate, a public sector investment entity might be required to report in accordance with IPSASs, IFRSs, or domestic standards. The IPSASB agreed that the IFRS 10 requirement for an investment entity to account for its investments at fair value appeared to be appropriate in the public sector. The IPSASB also noted that consistent requirements in IPSASs and IFRSs would reduce any opportunity for accounting arbitrage when determining which accounting standards an investment entity should be required to apply.
- BC22. The IPSASB considered whether the definition of an investment entity in IFRS 10 was appropriate in the public sector. The IPSASB agreed that the definition was largely appropriate although it noted that an investment entity will frequently have an external mandate that establishes its purpose (as opposed to the entity asserting its purpose to investors) and amended the definition accordingly. The IPSASB considered that it would be helpful to give additional public sector examples of scenarios in which an entity would not be an investment entity by virtue of having additional objectives.
- BC23. The IPSASB considered whether the typical characteristics of an investment entity were appropriate for application in the public sector. The IPSASB noted that IFRS 10 allows for the possibility that an entity may be an investment entity, despite not meeting all the typical characteristics. In such cases the entity is required to explain why it is an investment entity, despite not having all of the typical characteristics of an investment entity. The IPSASB considered that the typical characteristics identified in IFRS 10 were not likely to be typical characteristics in the public sector context. For example, a sovereign wealth fund might:
- (a) Have a single investor (being a Minister or a public sector entity). The fund could argue that it is investing funds on behalf of, or for the benefit of, citizens. IFRS 10, paragraph BC259, explicitly refers to government-owned investment funds and funds wholly owned by pension plans and endowments when explaining why the IASB decided to make this a typical characteristic rather than an essential part of the definition of an investment entity.
 - (b) Have investors that are related parties. A fund with a related party investor could nevertheless be acting on behalf of many unrelated beneficiary investors.
 - (c) Have ownership interests in a form other than equity or similar interests. The IPSASB noted both that the form of ownership interests in sovereign wealth funds could vary, and that IFRS 10, paragraph BC264, specifically refers to pension funds and sovereign wealth funds when explaining why the IASB decided to make this a typical characteristic rather than an essential part of the definition. IFRS 10, paragraph BC264, states "For example, a pension fund or sovereign wealth fund with a single direct investor may have beneficiaries that are entitled to the net assets of the investment fund, but do not have ownership units."
- BC24. Because of the differences between the private and public sector, the IPSASB decided not to identify typical characteristics separately from the definition of an investment entity. The IPSASB noted that much of the discussion in IFRS 10 regarding the typical characteristics of investment entities described ways in which an entity could demonstrate that it met the definition of an investment entity. The IPSASB therefore decided to retain such guidance, but to locate it together with other guidance on the definition of an investment entity. The IPSASB agreed that the characteristic in IFRS 10 that "The individuals or entities that have provided funds to the entity are not related parties of the entity" did not reflect the public sector context and agreed to omit the guidance on that characteristic.
- BC25. Although the IPSASB decided not to identify typical characteristics separately from the definition of an investment entity, the IPSASB considered that most public sector entities classifying themselves as investment entities should be required to disclose information about the judgments and assumptions made. The IPSASB considered that disclosure of these judgments and assumptions would be important for transparency and encourage appropriate use of the investment entity accounting requirements.
- BC26. The IPSASB noted that in comparison with private sector entities which tend to have clear financial objectives, public sector entities can have a broader range of objectives, and these objectives can change over time. A public sector entity's objectives may also change as a result of changes in government policy

and changes could lead to an entity that had formerly met the definition of an investment entity ceasing to do so. Having regard to the possibility of changing objectives the IPSASB therefore agreed to highlight the need for an entity to reassess its status on a regular basis.

- BC27. The IPSASB noted that the IFRS 10 investment entity requirements apply to the financial statements of an investment entity itself – they cannot be applied by the controlling entity of any investment entity. IFRS 10 requires that a controlling entity that is not itself an investment entity shall present consolidated financial statements in which all controlled entities are consolidated on a line by line basis. The IPSASB considered whether the public sector context would lead it to place more or less weight on arguments considered by the IASB in relation to this matter, and whether there were any public sector characteristics that would support a differing accounting treatment by the controlling entity of an investment entity.
- BC28. The IPSASB noted that the IASB had concerns that if a non-investment controlling entity were required to retain the fair value treatment used by its controlled investment entities, it could achieve different accounting outcomes by holding controlled entities directly or indirectly through a controlled investment entity. The IPSASB considered that this issue was of less concern in the public sector context. In particular the IPSASB noted that ownership interests through shares or other equity instruments are less common in the public sector. As a consequence, it is less likely that entities within an economic entity in the public sector would hold an ownership investment in the ultimate controlling entity and less likely that they would have ownership investments in other entities within the economic entity.
- BC29. The IPSASB considered what type of information users would find most useful about a controlled investment entity. The IPSASB considered that users would find it most useful if the accounting for investments applied in a controlled investment entity's financial statements were extended to its controlling entity's financial statements. The IPSASB therefore proposed that a controlling entity with a controlled investment entity should be required to present consolidated financial statements in which it (i) measures the investments of the controlled investment entity at fair value through surplus or deficit in accordance with IPSAS 29 and (ii) consolidates the other assets and liabilities and revenue and expenses of the controlled investment entity in accordance with the usual consolidation accounting policies required by the Standard. The IPSASB considered that its proposals reflect the fact that a controlling entity does not manage an investment entity itself on a fair value basis. Rather, it manages the investments of the investment entity on a fair value basis. This approach is also consistent with the accounting by an investment entity for its investments in other entities.
- BC30. At the time that IPSAS 35 was being developed the IASB proposed to clarify aspects of the application of the investment entity requirements. The IASB issued *Investment Entities: Applying the Consolidation Exception* (Amendments to IFRS 10, IFRS 12 and IAS 28) in December 2014. The IPSASB considered that these clarifications were helpful in addressing implementation issues identified by early adopters of the IASB's investment entity requirements and incorporated those aspects of the amendments that were relevant to this Standard.

Control (paragraphs 18–37)

- BC31. The IPSASB agreed that the three requirements for control outlined in IFRS 10 are generally appropriate for the public sector. The IPSASB noted that the IFRS 10 requirements to have power, returns and a link between power and returns is similar to the approach previously taken by the IPSASB in IPSAS 6, although IPSAS 6 required that both power and benefits be present. Consistent with the terminology used in IPSAS 6 the IPSASB decided that the term “benefits” was generally more appropriate than “returns” in the public sector context (as discussed under the subheading “Terminology” below). However, the term “returns” continued to be used in the context of investment entities.
- BC32. The IPSASB took note of the approach taken in Government Finance Statistics in relation to control over an entity. The 2008 SNA, paragraph 4.80, includes eight indicators of control of corporations and five indicators of control of nonprofit institutions and explains that “Although a single indicator could be sufficient to establish control, in other cases a number of indicators may collectively indicate control”. Overall, the direction of the statistical indicators is on the same lines as the approach in this Standard and therefore the practical results of the respective analyses will likely largely coincide. Some of the indicators in GFS are mentioned in the following paragraphs.

Power (paragraphs 23–29)

BC33. The IPSASB decided to modify IFRS 10 to:

- (a) Highlight the range of relevant activities that could occur in the public sector and stress that control of financial and operating policies can demonstrate power over relevant activities;
- (b) Clarify that regulatory control and economic dependence do not give rise to power for the purposes of the Standard; and
- (c) Discuss specific powers that could give rise to control in the public sector, including golden shares, a right to appoint the majority of the board of another entity, and powers obtained through legislation or enabling documents.

Regulatory Control

BC34. The IPSASB agreed that the previous guidance on regulatory control in IPSAS 6 should be incorporated in the Standard. The IPSASB noted that IFRS 10 had been developed for application by profit-oriented entities, few of whom have powers to create or enforce legislation or regulations. By contrast, the nature of government means that regulatory power occurs frequently in the public sector.

BC35. In considering how to incorporate guidance on regulatory control in the Standard the IPSASB noted that (i) the discussion of power in IFRS 10 focuses on the ability to influence the “relevant activities” of the investee, and (ii) power is only one of the three elements that are required for control to exist. The IPSASB decided to place the discussion of regulatory control alongside the discussion of power and relevant activities.

BC36. The IPSASB noted that the discussion of regulation and control in the 2008 SNA is similar to that previously in IPSAS 6. The 2008 SNA states:

Regulation and control. The borderline between regulation that applies to all entities within a class or industry group and the control of an individual corporation can be difficult to judge. There are many examples of government involvement through regulation, particularly in areas such as monopolies and privatized utilities. It is possible for regulatory involvement to exist in important areas, such as in price setting, without the entity ceding control of its general corporate policy. Choosing to enter into or continue to operate in a highly regulated environment suggests that the entity is not subject to control. When regulation is so tight as to effectively dictate how the entity performs its business, then it could be a form of control. If an entity retains unilateral discretion as to whether it will take funding from, interact commercially with, or otherwise deal with a public sector entity, the entity has the ultimate ability to determine its own corporate policy and is not controlled by the public sector entity.

BC37. The IPSASB noted that the 2008 SNA discusses control by a dominant customer. It states:

"In general, if there is clear evidence that the corporation could not choose to deal with non-public sector clients because of public sector influence, then public control is implied."

Economic Dependence

BC38. IFRS 10 paragraph B40 states that “...in the absence of any other rights, economic dependence of an investee on the investor (such as relations of a supplier with its main customer) does not lead to the investor having power over the investee.” Although the IPSASB agreed that economic dependence, on its own, does not give rise to control, the IPSASB noted that, in the public sector, economic dependence may occur in conjunction with other rights. These other rights need to be assessed to determine if they give rise to control.

BC39. Because of the prevalence of economic dependence in the public sector the IPSASB decided that it was appropriate to discuss ways in which economic dependence can arise and include examples of economic dependence.

Special Voting Rights Attaching to Ownership Interests (Golden Shares)

BC40. The IPSASB agreed that the Standard should acknowledge that special voting rights attaching to ownership interests (often referred to as “golden shares”) will influence assessments of control. The IPSASB noted that such rights are also acknowledged in the GFSM 2014.

Substantive Rights

BC41. Statutory independence is common in the public sector. The IPSASB agreed to illustrate the ways in which statutory independence may influence an investor’s assessments of rights. The Standard notes that

the existence of statutory independence of an investee could be seen as a barrier to the investor exercising its rights (paragraph AG26). It also notes that the existence of statutory powers to operate independently does not, of itself, preclude an entity from being controlled by another entity (paragraph 25).

Terminology

- BC42. In addition to making changes to reflect the standard terminology in IPSASs, the IPSASB agreed that a number of other changes to the terminology in IFRS 10 were appropriate. Unless noted otherwise in an IPSAS, this discussion of terminology is relevant to IPSASs 34 to 38.

Investor/Investee

- BC43. IFRS 10 uses the terms “investor” and “investee” to denote (i) the potential controlling entity, being the entity that is applying the Standard to assess whether control exists and (ii) the potential controlled entity. The IPSASB considered that these terms were inappropriate in most parts of this Standard because they could be read as implying the existence of a financial instrument representing an ownership interest. Most assessments of control in the public sector do not involve such financial instruments.
- BC44. The IPSASB considered other terms that could be used to describe investors and investees, in the context of the Standard. One option was to refer to an investor as a “potential controlling entity” and an investee as a “potential controlled entity”. The IPSASB considered that these phrases, whilst clear in meaning, would be cumbersome to use throughout the Standard. The IPSASB noted that IPSASs generally refer to the entity applying the Standard as “the entity”. In the case of this Standard, the entity applying the Standard is the entity that is assessing whether or not it controls another entity (referred to as the investor in IFRS 10). The entity applying the Standard is doing so in order to determine whether it controls another entity. The IPSASB therefore decided that, depending on the context, it would refer to the investor as “the entity” and the investee as “another entity”, “other entity”, or “entity being assessed for control”.
- BC45. The IPSASB agreed to retain use of the term “investors” where the Standard is referring to a specific investment and the term is used in accordance with its usual meaning. This was particularly relevant in the parts of the Standard dealing with investment entities.
- BC46. The IPSASB also agreed that the terms “investor” and “investee” are appropriate when referring to interests in joint ventures and associates.

Binding Arrangements

- BC47. The IPSASB agreed to replace most references to “contractual arrangements” in IFRS 10 with references to the term “binding arrangements”. This change acknowledges that in some jurisdictions, entities applying IPSASs may not have the power to enter into contracts but nevertheless may have the authority to enter into binding arrangements. In addition, the IPSASB agreed that binding arrangements, for the purpose of this Standard, should encompass rights that arise from legislative or executive authority. The definition of binding arrangements used in this Standard is intentionally broader than that used in the financial instruments standards, where it is used in relation to rights that are similar to contracts and in respect of willing parties.

Benefits

- BC48. The IPSASB agreed that the term “benefits” is more appropriate than the term “returns” in the public sector, particularly given the existence of control relationships in the absence of a financial investment in the controlled entity. The IPSASB considered that the term “returns” could be regarded as giving an inappropriate emphasis to financial returns, whereas, in the public sector, benefits are more likely to be non-financial than financial. The term “returns” was retained in the context of investment entities.
- BC49. The IPSASB decided to modify IFRS 10 to:
- (a) Highlight that many assessments of control in the public sector involve assessments of non-financial benefits;
 - (b) Note that benefits can have positive or negative aspects; and
 - (c) Include examples of benefits in a public sector context.

- BC50. The IPSASB agreed to locate the examples of benefits in the body of the Standard as it considered that the examples would be particularly useful for an entity making an initial assessment of whether it might control other entities.
- BC51. The definition of control in IPSAS 35 refers to “variable benefits” and this concept is referred to throughout the Standard. The IPSASB considered how the Standard would apply to benefits that appeared to be fixed or constant. The IPSASB noted that the IASB had explicitly considered this issue and had provided examples to show that benefits that appear to be fixed could in fact be variable, because they exposed the entity to performance risk. The IPSASB noted that the IASB examples related to financial benefits and agreed to incorporate an example of a non-financial benefit in paragraph AG58.

Uniform Reporting Dates

- BC52. The IPSASB considered whether to impose a time limit on the difference between the end of the reporting period of the controlling entity and its controlled entities. The IPSASB noted that IFRS 10 requires that the financial statements used in preparing consolidated financial statements have the same reporting date, or where this is impracticable, requires that adjustments be made to the most recent financial statements of the controlled entities. In addition, IFRS 10 limits the difference in dates to three months. The IPSASB noted that there may be instances in the public sector where entities have different reporting dates and it may not be possible to change those dates. The IPSASB agreed not to impose a three month limit on the difference in dates.

Implementation Issues

- BC53. A number of respondents commented on the difficulty of preparing consolidated financial statements, particularly when there are a large number of controlled entities, as in the case of whole of government financial statements. The IPSASB acknowledged these practical difficulties, whilst noting that most jurisdictions presenting consolidated financial statements have faced similar difficulties. In these jurisdictions the consolidating entities used simplifying strategies to cope with the complexity and the consolidation difficulties. Such strategies include:
- (a) Assessing the existence of control for various categories of entities in phases, with an initial focus on entities that are likely to be material.
 - (b) Not consolidating (or deferring the consolidation of) controlled entities that are likely to be immaterial.
 - (c) Identifying the cost-effective ways of obtaining information about inter-entity balances and transactions.
 - (d) Not eliminating immaterial inter-entity transactions and balances.
 - (e) Considering whether all disclosures must be made in respect of all entities.
- BC54. The IPSASB considered whether to provide specific guidance on the application of materiality when preparing consolidated financial statements but concluded that this would not be appropriate in a financial reporting standard.

Sale or Contribution of Assets between an Investor and its Associate or Joint Venture

- BC55. At the time that IPSAS 35 was being developed, the IASB was in the process of seeking feedback on proposals to amend IFRS 10 and IAS 28 so that the requirements for the recognition of a partial gain or loss for transactions between an investor and its associate or joint venture would apply only to the gain or loss resulting from the sale or contribution of assets *that do not constitute a business*, as defined in IFRS 3, *Business Combinations*. The IASB issued *Sale or Contribution of Assets between an Investor and its Associate or Joint Venture* (Amendments to IFRS 10 and IAS 28) in September 2014. The IPSASB agreed not to incorporate the requirements introduced by these amendments in IPSAS 35 and IPSAS 36, *Investments in Associates and Joint Ventures*, on the grounds that it would be more appropriate to consider the recognition of full or partial gains and losses in the context of drafting standards-level requirements for public sector combinations.
- BC56. At the time the IPSASB developed ED 60, *Public Sector Combinations*, it reconsidered whether to include guidance on how to account for the loss of control of a former controlled entity to an investor’s associate or joint venture. The IPSASB reviewed the guidance issued by the IASB in *Sale or Contribution of Assets between an Investor and its Associate or Joint Venture* (Amendments to IFRS 10 and IAS 28). The effect

of the IASB's amendments if adopted in IPSAS 35 would be that a partial gain or loss for transactions between an investor and its associate or joint venture would apply only to the gain or loss resulting from the loss of control of a former controlled entity *that does not contain an operation*. The IPSASB did not identify any public sector reason to depart from the IASB's approach. Consequently, the IPSASB agreed to include this guidance (amended to fit the terminology and definitions in ED 60) in IPSAS 35.

- BC57. In December 2015, the IASB deferred the implementation of the guidance in *Sale or Contribution of Assets between an Investor and its Associate or Joint Venture* (Amendments to IFRS 10 and IAS 28). This was because the IASB was undertaking further research in this area as part of its project on equity accounting, and it did not want to require entities to change their accounting twice in a short period. In deferring the effective date, the IASB continued to allow early application of the guidance as it did not wish to prohibit the application of better financial reporting. The IPSASB reviewed the decision of the IASB to defer the implementation of this guidance. The IPSASB did not identify any public sector reason to depart from the IASB's approach. Consequently, the IPSASB agreed to include this guidance (amended to fit the terminology and definitions in IPSAS 40) in IPSAS 35, to be applied from a date to be determined by the IPSASB.

Revision of IPSAS 35 as a result of the IPSASB's *The Applicability of IPSASs*, issued in April 2016

- BC58. The IPSASB issued *The Applicability of IPSASs* in April 2016. This pronouncement amends references in all IPSASs as follows:

- (a) Removes the standard paragraphs about the applicability of IPSASs to "public sector entities other than GBEs" from the scope section of each Standard;
- (b) Replaces the term "GBE" with the term "commercial public sector entities", where appropriate; and
- (c) Amends paragraph 10 of the *Preface to International Public Sector Accounting Standards* by providing a positive description of public sector entities for which IPSASs are designed.

The reasons for these changes are set out in the Basis for Conclusions to IPSAS 1.