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Dear Stephenie,

COMMENT ON THE EXPOSURE DRAFTS ON ACCOUNTING FOR INTERESTS IN OTHER ENTITIES

We welcome the opportunity to comment on the following Exposure Drafts:

- ED 48 *Separate Financial Statements*;
- ED 49 *Consolidated Financial Statements*;
- ED 50 *Investments in Associates and Joint Ventures*;
- ED 51 *Joint Arrangements*; and
- ED 52 *Disclosure of Interests in Other Entities*.

Overall, we support the development of the Exposure Drafts as we believe that they provide a comprehensive set of principles to be used by entities in accounting, reporting and disclosing their interests in other entities.

Some of our stakeholders noted that the IASB has a number of projects on its work programme that consider amendments to its suite of Standards that deal with interests in other entities, which may impact the IPSASB's project. An example is the recent Exposure Draft that requested comment on reinstating the option to use the equity method to account for investments in controlled entities, associates and joint ventures in an entity's separate financial statements. We propose that the IPSASB consider the outcome of these amendments before finalising its project on interests in other entities.

Board Members: Mr V Jack (Chairperson), Ms T Coetzer, Mr B Colyvas, Ms CJ Kujenga,
Mr K Kumar, Mr K Makwetu, Mr G Paul, Ms N Ranchod, Ms R Rasikhinya,
Alternates: Ms L Bodewig, Mr J Van Schalkwyk
Chief Executive Officer: Ms E Swart



Our comment to you is set out in two parts: Part I outlines comment to the specific matters for comment and Part II outlines general comment on some of the principles included in the Exposure Drafts.

The comment on the Exposure Drafts is that of the Secretariat of the Accounting Standards Board and not that of the Board. In formulating our comment on the Exposure Drafts, the Secretariat consulted with a range of stakeholders including auditors, preparers, consultants, professional bodies and other interested parties.

Please feel free to contact me should you require clarification on any of our comments.

Yours sincerely

A handwritten signature in blue ink that reads "Erna Swart". The signature is written in a cursive style with a small dot at the end.

Erna Swart, Chief Executive Officer

PART I – RESPONSES TO SPECIFIC MATTERS FOR COMMENT

Exposure Draft 48, *Separate Financial Statements*

Specific Matter for Comment 1

Do you agree generally with the proposals for separate financial statements? In particular, do you agree with the proposal to permit the use of the equity method, in addition to cost or fair value, for investments in other entities?

We agree with the proposals for separate financial statements as included in Exposure Draft 48. We are of the view that the Exposure Draft provides adequate guidance with regards to accounting and disclosure requirements when an entity prepares separate financial statements.

Use of the Equity Method

The equity method is a well-established, acceptable method of accounting. As the equity method represents a valuation methodology for investments based on increases, or decreases, of the assets and liabilities of the controlled entity, associate or joint venture, it provides useful information to the users of the financial statements about the performance of these investments. We therefore agree with the proposal to permit the use of the equity method in addition to cost or fair value, in accounting for investments in controlled entities, associates and joint ventures in an entity's separate financial statements.

However, the IPSASB should consider the extent to which comparability between entities may be impaired when allowing three methods to present information about an investment in other entities in an entity's separate financial statements. In particular, the IPSASB should consider whether the qualitative characteristics in the Conceptual Framework, specifically comparability, will be met.

In addition, as mentioned in the covering letter, we recommend that the IPSASB consider the outcome of the IASB's project before approving the Standard.

Exposure Draft 49, Consolidated Financial Statements

Specific Matter for Comment 1

Do you agree with the proposed definition of control? If not, how would you change the definition?

We agree with the proposed definition of control as included in the Exposure Draft. We do, however, have a few suggestions in applying the definition to specific circumstances. These are included in Part II.

Specific Matter for Comment 2

Do you agree that a controlling entity should consolidate all controlled entities (except in the circumstances proposed in this Exposure Draft)?

If you consider that certain categories of entities should not be consolidated, please justify your proposal having regard to user needs and indicate your preferred accounting treatment for any such controlled entities. If you have any comments about temporarily controlled entities, please respond to Specific Matter for Comment 3.

We agree that a controlling entity should consolidate all its controlled entities, as including all entities in the consolidation will provide a complete and useful assessment of the economic entity's activities and current financial position.

Specific Matter for Comment 3

Do you agree with the proposal to withdraw the exemption in IPSAS 6, Consolidated and Separate Financial Statements (December 2006) for temporarily controlled entities?

If you agree with the withdrawal of the exemption please give reasons. If you disagree with the withdrawal of the exemption please indicate any modifications that you would propose to the exemption in IPSAS 6 (December 2006).

We agree with the proposal to withdraw the exemption in IPSAS 6, *Consolidated and Separate Financial Statements* (December 2006) relating to temporarily controlled entities. We have noted that in many instances it takes more than twelve months to dispose of a temporarily controlled entity, as legislation and other requirements have to be met before a sale is concluded, despite management's intention to sell the entity within a twelve month period. We also acknowledge that in many instances, judgment has to be applied in determining whether an entity should be classified as temporarily controlled. By excluding these entities from the consolidation, we are of the view that fair presentation, relevance and the reliability of the financial statements may have been impaired.

We do have proposals for disclosures that could be included in the financial statements where management intends to sell a controlled entity. These proposals have been included in our response to specific matter for comment 1 on Exposure Draft 52.

Specific Matter for Comment 4

Do you agree that a controlling entity that meets the definition of an investment entity should be required to account for its investments at fair value through surplus or deficit?

We agree that a controlling entity that meets the definition of an investment entity should be required to account for its investments at fair value through surplus or deficit. Accounting for investments at fair value through surplus and deficit:

- (a) enhances the comparability of the different investments reported in an investment entity's financial statements;
- (b) provides useful information to the users of the financial statements as the method of accounting for these investments reflects the way in which they are managed, i.e. on a fair value basis.

Specific Matter for Comment 5

*Do you agree that a controlling entity, that is not itself an investment entity, but which controls an 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, *Financial Instruments: Recognition and Measurement*, and (ii) consolidates the other assets and liabilities and revenue and expenses on the controlled investment entity in accordance with this Standard?*

Do you agree that the proposed approach is appropriate and practicable? If not, what approach do you consider would be more appropriate and practicable?

We agree that a controlling entity, that is not itself an investment entity, but which controls an 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, *Financial Instruments: Recognition and Measurement*, and (ii) consolidates the other assets and liabilities and revenue and expenses on the controlled investment entity in accordance with this Exposure Draft.

We support the IPSASB's view that extending the accounting for investments in a controlled investment entity's financial statements to its controlling entity's financial statements, would provide the users of the financial statements with useful information.

Specific Matter for Comment 6

The IPSAS has aligned the principles in this Standard with the Government Finance Statistics Manual 2013 (GFSM 2013) where feasible. Can you identify any further opportunities for alignment?

We have not identified any further opportunities for alignment between the principles in this Standard and GFSM 2013.

Exposure Draft 50, *Investments in Associates and Joint Ventures*

Specific Matter for Comment 1

Do you generally agree with the proposals in the Exposure Draft? If not, please provide reasons.

We agree with the proposals in the Exposure Draft in general. We have, however, included comment on certain principles in this Exposure Draft in Part II of our response.

Specific Matter for Comment 2

Do you agree with the proposal that the scope of the Exposure Draft be restricted to situations where there is a quantifiable ownership interest?

We agree that the scope of the Exposure Draft should be restricted to quantifiable ownership interest.

The second sentence in paragraph .04 of this Exposure Draft determines that the Standard applies to quantifiable ownership interest, which includes interests that arises from a formal equity structure. The rest of this paragraph and paragraph .05 then includes explanatory guidance on what a formal equity structure constitutes. However, in reading BC 5, quantifiable ownership interest, in our view, also includes other forms like partnership arrangements which do not have formal equity structures.

We are of the view that the inclusion of the scope restriction has narrowed the scope for joint ventures, whom in many instances, may not have a formal equity structure. As the explanations in paragraphs .03 to .05 are limited to a discussion of a formal equity structure, entities that have other structures such as partnership arrangements, may conclude that they fall outside the scope of this Exposure Draft, if the explanation in the Exposure Draft is limited to a discussion of a formal equity structure

We are of the view that more explanatory guidance should be included to explain that entities with structures such as partnership arrangements may also apply the principles in this Exposure Draft, even though there are no formal equity structure.

An example could also be included to explain the concept of quantifiable ownership interest.

We propose that the explanation of quantifiable ownership interest could be expanded to refer to binding arrangements.

We also propose that when an entity falls outside the scope of this Exposure Draft because it does not have a quantifiable ownership interest, the Exposure Draft should refer preparers to the relevant IPSASs that should be applied.

Specific Matter for Comment 3

Do you agree with the proposal to require the use of the equity method to account for investments in joint ventures? If not, please provide reasons and indicate your preferred treatment.

We agree with the proposal to only require the use of the equity method to account for investments in joint ventures. We support the view that the equity method better reflects the rights and obligations of an entity as a result of its interest in the arrangement, regardless of its structure or legal form.

Exposure Draft 51, *Joint Arrangements*

Specific Matter for Comment 1

Do you agree that joint arrangements should be classified as joint ventures or joint operations based on whether an entity has (i) rights to assets and obligations for liabilities, or (ii) rights to net assets?

We agree with the proposed classification of a joint arrangement based on an entity's rights to assets and/or obligations for liabilities, or its rights to net assets.

Specific Matter for Comment 2

Do you agree that joint ventures should be accounted for in consolidated financial statements using the equity method?

As with our response to specific matter for comment 3 in Exposure Draft 50, we agree with the proposal to only require the use of the equity method to account for investments in joint ventures.

Exposure Draft 52, *Disclosure of Interests in Other Entities*

Specific Matter for Comment 1

Do you agree with the proposed disclosures in this draft Standard? If not, why? Are there any additional disclosures that would be useful to users of financial statements?

We agree with the proposed disclosures in this Exposure Draft.

However, we propose that some disclosure requirements should be included for temporarily controlled entities held for sale in the absence of an IPSAS that deals with non-current assets held for sale.

We propose that the following disclosures should be considered for material temporarily controlled entities, associates or joint ventures, and in aggregate for immaterial temporarily controlled entities, associates or joint ventures:

- a description of the temporarily controlled entity, associate or joint venture and the rationale for its acquisition;
- the carrying value of the assets and liabilities that will be affected by the disposal of the temporarily controlled entity, associate or joint venture; and
- a description of the intended manner of disposal, including the expected sale or transfer date.

We are of the view that these disclosures will provide useful information for decision making to the users of the financial statements.

Specific Matter for Comment 2

Do you agree with the proposal that entities for which administrative arrangements or statutory provisions are dominant factors in determining control of the entity are not structured entities? If not, please explain why and explain how you would identify entities in respect of which the structured entity disclosures would be appropriate.

The definition in paragraph .07 refers to those circumstances where administrative arrangements and legislation are not normally the dominant factors. We are of the view that entities will find it difficult to identify a public sector structured entity based on this definition, and therefore propose that explanatory guidance should be included in the Exposure Draft to explain the definition. Furthermore, illustrative examples should be included in the Exposure Draft to assist preparers with the identification of a structured entity.

We also question how a binding arrangement, as referred to in Exposure Draft 50 and Exposure Draft 51, will impact the definition and identification of a structured entity. In the explanation in AG20, reference is made to both administrative arrangements and binding arrangements, yet the definition of a structure entity only refers to administrative arrangements. Clarification on how or whether binding arrangements are considered in identifying structured entities should be provided in this Exposure Draft.

Furthermore, the guidance provided in AG22(c) and (d) should be reconsidered as it is, in our view, not public sector specific.

PART II – OTHER COMMENTS

Exposure Draft 48, Separate Financial Statements

1. Definitions

We agree with the definitions that have been included in the Exposure Draft, but propose that the following additional definitions, which are currently only included in Exposure Draft 49, also be included in this Exposure Draft:

- Controlled entity,
- Controlling entity,
- Equity method; and
- Investment entity.

Because the scope of this Exposure Draft is limited to an entity that prepares and presents separate financial statements, we are of the view that including these definitions will be useful to the preparers of the financial statements, specifically in those circumstances where an entity does not present consolidated financial statements.

This Exposure Draft includes transitional provisions for investment entities, and in understanding, from a preparer's perspective, whether these provisions should be applied or considered, preparers will find an explanation of the term "investment entity" useful.

2. Transitional relief relating to an investment entity

The IPSASB's Exposure Draft on *Consolidated Financial Statements* (ED 49) introduced the concept of investment entities.

This Exposure Draft requires an investment entity to retrospectively adjust the measurement of its investment entity that was previously measured at cost, to fair value through surplus and deficit. In considering the cost-benefit criterion, and based on the availability of information on the date adoption of accrual basis IPSASs, we are of the view that relief should be provided to first-time adopters in accounting for their investments entities by allowing them to determine fair value on the date of transition to accrual basis IPSASs.

3. Initial application

Paragraph 23 of this Exposure Draft includes the transitional requirements that should be applied on initial application of this pronouncement. The term used in the heading "initial application" is, however, not consistent with the terminology usually used in other IPSASs. We therefore propose that the heading to paragraph 23 should be amended to "transitional provisions" to achieve consistency.

In addition, we also propose that the paragraph should be clarified to require that an investment entity that is a controlling entity (as envisaged in Exposure Draft 49.52) and an investment entity that is a controlled entity (as envisaged in Exposure Draft 49.54), apply these transitional provisions.

4. Cross reference to information dealing with separate financial statements in other Exposure Drafts

Paragraph .41 of Exposure Draft 51 sets out the transitional provisions to be applied in an entity's separate financial statements for interests in joint operations. We propose that the IPSASB should reconsider the positioning of this guidance as in our view, it should be included in the pronouncement that provides guidance on separate financial statements. This will also ensure that the IPSASB meets its objective of presenting all the requirements relating to separate financial statements, in one IPSAS. Alternatively, the IPSASB could include a cross reference between Exposure Draft 51 and Exposure Draft 48 so that preparers could consider all the applicable principles in presenting its separate financial statements.

Exposure Draft 49, Consolidated Financial Statements

5. Scope

Whole-of-government consolidations

Paragraph .03 of this Exposure Draft explains when consolidated financial statements shall be presented. Even though whole-of-government is defined differently in various jurisdictions, we are of the view that preparers would find an explanation around the application of the principles to the preparation of whole-of-government financial statements useful. As such, we propose that the scope of this Exposure Draft should be expanded to clarify the application to whole-of-government consolidations, similar to the existing guidance that is included in IPSAS 6.17 and .18.

Consolidation exemptions

We propose that the wording in paragraph 5(c) should be amended to clarify that the exemption from preparing consolidated financial statements can only be applied, if an investment entity measures its investments in a controlled entity at fair value through surplus and deficit as determined in paragraph .52. At present, it may be interpreted to be an option.

We propose the following change:

“An investment entity reporting in accordance with IPSASs need not present consolidated financial statements if it measures all of its investments in a controlled entity at fair value through surplus and deficit as required by paragraph .52 of this Standard. ~~if it is required, in accordance with paragraph 52 of this Standard, to measure all of its controlled entities at fair value through surplus or deficit.~~”

6. Explanatory guidance in meeting the definition of control

The exposure or right to benefits from the entity's involvement with the other entity is one of the criteria needed in meeting the definition of control. This Exposure Draft explains the other two criteria that need to be met in order for control to exist in paragraphs .19 to .30, but no explanation is given about the entity's exposure, or its rights to benefits, including its assessment of substantive and protective rights. The Application guidance includes detail guidance around the various rights that an entity can have. In understanding the second criteria in the control definition, we propose that the IPSASB should include a general paragraph in the Exposure Draft itself, to explain these aspects. We also recommend that 'political rights' need to be explained, along with an indication as to whether or not it should be considered in meeting the definition of control. The principles should be in the standard itself. The application guidance cannot extend the principles; it should illustrate the application.

Furthermore, IPSAS 6.36 includes explanatory guidance about an entity's ability to govern decision-making in relation to the financial and operating policies of another entity, and how it impacts on meeting the definition of control. We are of the view that this explanation is useful in understanding whether control is met in those circumstances where a controlling entity cannot demonstrate that it governs decision-making over the controlled entity's financial and operating policies. We, therefore, propose that a similar explanation should be included in the Exposure Draft.

7. Guidance when the definition of control is not met

Paragraphs .14 to .16 of this Exposure Drafts explain the control criteria, and require that all three elements need to be met for an entity to prepare consolidated financial statements. We propose that this Exposure Draft should include a reference to the appropriate accounting guidance that should be considered when an entity concludes that it does not have control over another entity.

8. Non-financial benefits

Paragraphs .26, .27 and .29 of this Exposure Draft include examples of non-financial benefits. Some of our stakeholders questioned the relationship between the concept of service potential and non-financial benefits. We therefore propose that an explanation should be included in this Exposure Draft explaining service potential, and how it relates to non-financial benefits.

9. Different reporting periods

Paragraph B93 of IAS 10 requires that the difference between the end of the reporting period of the controlled entity and the controlling entity should not be more than three months.

The IPSASB has not included a similar requirement in this Exposure Draft, but rather requires that adjustments should be made for the effects of significant transactions or events between the date of the financial statements of the controlled and controlling entity. However, the IPSASB's rationale for including a different requirement in this Exposure Draft is not explained in the Basis for Conclusions. We therefore recommend that the Basis for Conclusions be amended to explain the IPSASB's decision.

10. Implementation Guidance

We question the public sector relevance of example 7 of an investment vehicle, example 51 of a real estate entity and example 52 of a master fund. We propose that more relevant public sector specific examples should be included to assist preparers in understanding and in identifying an investment entity.

Exposure Draft 50, *Investments in Associates and Joint Ventures*

11. Definitions

We agree with the definitions that have been included in the Exposure Draft, but as with our general comment to Exposure Draft 48, we are of the view that the definition for “investor” and “investee” should be included in this Exposure Draft as it would be useful to the preparers of the financial statements.

12. Different reporting periods

IAS 28.34 requires that the difference between the end of the reporting period of the associate or joint venture, and that of the entity should not be more than three months.

The IPSASB has not included a similar requirement in this Exposure Draft, but rather requires that adjustments should be made for the effects of significant transactions or events between the date of the financial statements of the associate or joint venture, and that of the entity. The IPSASB’s rationale for including a different requirement in this Exposure Draft is not explained in the Basis for Conclusions. We therefore propose that the Basis for Conclusions should be amended to explain the decision.

13. Impairment losses

Paragraph .45 includes detail guidance on how an entity should apply the principles in IPSAS 26 to determine whether its net investment in an associate or joint venture, is impaired, whereas paragraph .46, merely explains the principles and terminology in IPSAS 21.

We question whether the guidance in paragraphs .45 and .46 are needed, as we believe that the reference to IPSAS 21 and IPSAS 26 in paragraph .44 is sufficient. We therefore propose that paragraphs .45 to .46 should be deleted.

14. Cross reference to transitional provisions following the elimination of proportionate consolidation

Paragraph .32 of Exposure Draft 51 sets out the transitional provisions to be applied in the transition from proportionate consolidation to the equity method. We propose that the IPSASB should consider including a cross reference in this Exposure Draft to the transitional guidance in Exposure Draft 51.

15. Effective date paragraph

As with the other Exposure Drafts that deal with interests in other entities, we propose that the first effective date paragraph should be in bold text.

Exposure Draft 51, *Joint Arrangements*

16. Sequence of the Exposure Drafts

We propose that the IPSASB reconsider the sequence and numbering of the paragraphs in that deals with the accounting of associates and joint ventures. This Exposure Draft assists users to identify whether an arrangement should be classified as a joint operation and joint venture. In our view, this would be the first step to follow, before accounting for the arrangement Exposure Draft 50 would be considered.

17. Determining joint control

Paragraph .07 defines joint control as the agreed sharing of control of an arrangement by way of a binding arrangement, which exists only when decisions about the relevant activities requires unanimous consent of the parties sharing the control. Exposure Draft 49 explains how and whether control exists where a public sector entity is carrying out government policy on behalf of an executive authority (AG 59). We propose that similar guidance should be included in this Exposure Draft to illustrate whether joint control exists where government policy are carried out in terms of an arrangement.

18. Financial statements of parties to a joint arrangement

Paragraph .23(c) and (d) makes reference to “sale”, which in our view, reflects private sector circumstances. The requirements in this paragraph should also be expanded to non-exchange revenue transactions, and we propose that the paragraph should be extended to also refer to distributions made at no or nominal value.

19. Cross reference to information dealing with separate financial statements

Paragraph .41 of this Exposure Draft sets out the transitional provisions to be applied in an entity’s separate financial statements for interests in joint operations. As we have mentioned in our general comments to Exposure Draft 48 above, we propose that the IPSASB should reconsider the positioning of this guidance. In our view, it should be included in the pronouncement that provides guidance on separate financial statements. Alternatively, the IPSASB should consider including cross references between this Exposure Draft and Exposure Draft 48.

20. Cross reference to transitional provisions following the elimination of proportionate consolidation

Paragraph .32 of this Exposure Draft sets out the transitional provisions to be applied in the transition from proportionate consolidation to the equity method. We propose that the IPSASB should consider including a cross reference to Exposure Draft 50 that deals with the accounting of joint ventures.

21. Illustrative examples

Example 1 illustrates the application of this Exposure Draft to a construction service between a private sector entity and a public sector entity. Some of our stakeholders questioned how this example impacts the application of the IPSAS on *Service Concession Arrangements: Grantor* (IPSAS 32). We therefore propose that the link between this example and IPSAS 32 should be clarified.

Exposure Draft 52, *Disclosure of Interests in Other Entities*

22. Inclusion of disclosures in reports that are not part of the financial statements

Paragraph .12 of this Exposure Draft requires disclosures about the methodology applied by an entity to determine whether control, joint control or significant influence exists over another entity. Paragraph 13 allows the entity to include these assumptions and methodology either in the financial statements, or by means of a cross reference to some other statement that is available to users of the financial statements.

We question the requirement to allow the inclusion of a cross reference to another statement based on the requirements in paragraph .136 of IPSAS 1 that requires an entity to disclose, as part of the summary of significant accounting policies or other notes, judgment that was applied by management to the extent that it has a significant effect on amounts recognized in the financial statements.

As a result, we propose that the requirement in paragraph .13 should be amended to require disclosure in the financial statements.

23. Disclosures around the nature of interests and risks

Paragraphs .45 and .46 require an entity to disclose information about the nature of interests and the nature of risks, in tabular format. We question why the format is prescribed in these two paragraphs only. For example, the presentation of the disclosures about the nature of risks associated with an entity's interest in consolidated structured entities (paragraphs .21 – .24) and the nature and extent of interests in joint arrangement and associates (paragraphs .36 - .39), are not that prescriptive.

We therefore propose that the IPSASB should reconsider the requirement to present the information in a table.