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Advancing Government Accountability

2208 Mount Vernon Ave.
Alexandria, VA 22301-1314
PH 703.684.6931
TF 800.AGA.7211
FX 703.548.9367
www.agacgfm.org

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Ms. Stephanie Fox
Technical Director
International Public Sector Accounting Standards Board
International Federation of Accountants
277 Wellington Street West, 6th Floor
Toronto, Ontario M5V 3H2 CANADA

Dear Ms. Fox:

On behalf of the Association of Government Accountants (AGA), the Financial Management Standards Board (FMSB) appreciates the opportunity to provide comments to the International Public Sector Accounting Standards Board (IPSASB) on its June 2012 Consultation Paper (CP) entitled *Public Sector Combinations*. The FMSB is comprised of 25 members (list attached) with accounting and auditing backgrounds in federal, state and local government, as well as academia and public accounting. The FMSB reviews and responds to proposed standards and regulations of interest to AGA members. Local AGA chapters and individual members are also encouraged to comment separately.

The FMSB believes that the need for guidance in the arena of public sector combinations is important and necessary. Negative world-wide economic conditions and the impact such conditions have on government budgets have caused and will continue to cause governments to rethink such basic issues as how services are provided, who provides services and the most efficient way to provide services. It is very likely that such conditions and such efforts will result in government operations being restructured. The IPSASB's efforts to address these issues are critical and will help to ensure that accounting for such transactions is consistent and that the results are useful. The FMSB supports the approach suggested in the Consultation Paper of accounting for such transactions as either an acquisition or an amalgamation. This is similar to an approach recently proposed by GASB in their recent exposure draft on this topic where it was proposed that transaction be accounted for as either an acquisition or a merger. For both GASB and IPSAB, the presence of consideration is a factor in determining whether an acquisition has taken place. For GASB, the presence of consideration is the determining factor; for IPSASB it is a characteristic among others to be considered (IPSASB, par. 3.11).

The FMSB does have a concern regarding one aspect of the Consultation Paper's approach for classifying transactions as either an acquisition or an amalgamation. The Consultation Paper defines an amalgamation as "… a transaction or other event where (a) two or more operations combine, (b) none of the combining operations gain control of the other operations, and (c) the transaction or other event is not the formation of a joint venture." The FMSB believes that the key aspects of the definition will be subpart (b) dealing with the issue of control, and that using control to classify transactions may be problematic.

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An example of this difficulty is presented Section 3, “The Boundary between Acquisitions and Amalgamations.” Paragraphs 3.2 and 3.12 provide that an amalgamation that occurs when a combination is imposed on one level of government, call it A, by another level of government, call it B, even though B does not control A. The CP states that the imposition is possible because B can direct A to do it. It seems to us that the ability to direct the action of A is an indication of control. Moreover, other characteristics are listed in paragraph 3.13 that also may be present in a combining transaction that might tip the balance towards the transaction being classified as an acquisition. We are concerned that few transactions shall be balanced in such a way that one entity may not have some advantage over another entity in size or representation in the new amalgamated entity when the transaction has been completed. While we recognize that professional judgment shall be involved in any such determinations, we would suggest that the IPSASB provide some additional guidance in this regard.

An alternative to the IPSASB’s approach would be to adopt an approach similar to GASB’s proposal to classify transactions based upon the exchange (or lack of an exchange) of significant consideration between the entitys in the transaction. This type of monetary approach to classifying transactions would result in a simpler classification approach than the approach suggested in the Consultation Paper and eliminate the need to discuss the issue of Not Under Common Control (NUCC) and Under Common Control (UCC). As we reviewed the Consultation Paper, we found that if approach B is adopted related to acquisitions, there is little distinction between the accounting treatments for most transactions, except for an acquisition where consideration has been exchanged. The accounting for amalgamations and acquisitions without consideration seems to be on a similar basis and adds a level of complexity to the accounting issues that may not be warranted.

Following are the FMSB’s response to the areas for specific comment.

1. In your view, is the scope of this CP appropriate?

FMSB Response: We believe that the scope of the CP is appropriate to address the matter of Public Sector Combinations.

2. In your view, is the approach used in this CP of distinguishing between acquisitions and amalgamations, with a further distinction for PSCs NUCC and UCC, appropriate? If you do not support this approach, what alternatives should be considered? Please explain your reasoning.

FMSB Response: The approach outlined in the CP provides an approach for classifying transactions that does reach the goal desired by the IPSASB. However, as stated in our general comments on the preceding page, we believe that the IPSASB should consider adopting a framework for classifying the transaction as either an acquisition or an amalgamation using criteria similar to that used by GASB in its recent exposure draft on public sector combinations. The approach used by GASB was centered on the concept of whether or not the transaction involved the exchange of significant consideration, rather than whether or not one entity obtained control over another entity. This approach also appears to align with the accounting approach suggested in the Consultation Paper if Alternative B for acquisitions is used. In this approach, only transactions that involves the exchange of consideration will result in items being recognized at “fair value”. In all other instances, the use of “carrying values” is the suggested method for recording transactions. It would seem logical to align the accounting with the classification of the transactions. Furthermore, the matter of classifying a transaction as an acquisition when the entities that are combining operations are themselves under common control (UCC) and no significant consideration was exchanged seems to be incongruent with the nature of the underlying transaction. If the entities are already under common control, this would appear to be an amalgamation (or merger) rather than an acquisition.

3. In your view, are there other public sector characteristics that should be considered in determining whether one party has gained control of one or more operations?

FMSB Response: As suggested in our general comments, we would prefer if the IPSASB focused its classification of the transaction as either an acquisition or an amalgamation on the presence of significant consideration rather than a matter of control after the combination is complete.

4. In your view, should the recipient in an acquisition NUCC recognize in its financial statements, the acquired operation's assets and liabilities by:

> (a) Applying fair value measurement to the identifiable assets acquired and liabilities assumed in the operation at the date of acquisition for all acquisitions (Approach A);
> (b) Distinguishing between different types of acquisitions (Approach B) so that:
> (i) For acquisitions where no or nominal consideration is transferred, the carrying amounts of the assets and liabilities in the acquired operation's financial statements are recognized, with amounts adjusted to align the operation's accounting policies to those of the recipient, at the date of acquisition; and
> (ii) For acquisitions where consideration is transferred, fair value measurement is applied to the identifiable assets acquired and liabilities assumed in the operation, at the date of acquisition; or
> (c) Another approach?

Please explain why you support Approach A, Approach B or another approach.

FMSB Response: The FMSB supports approach B in accounting for acquisitions. We believe that where significant consideration has been exchanged, an acquisition has been executed and the transaction should be accounted for using a fair value measurement approach. We believe that this aligns the accounting with fundamental nature of the transaction.

5. In your view, where the consideration is in excess of the net assets acquired, should the difference arising in an acquisition NUCC (for both Approach A and Approach B, acquisitions where consideration is transferred) be recognized in the recipient's financial statements, on the date of acquisition, as:

> (a) Goodwill for acquisitions where the acquired operation is cash-generating and a loss for all other acquisitions;
> (b) Goodwill for all acquisitions (which would require development of a definition of goodwill that encompasses the notion of service potential); or
> (c) A loss for all acquisitions?

Please explain why you support (a), (b), or (c).

FMSB Response: We believe that where necessary a gain or a loss should be recognized in all cases so long as the gain or loss is computed using fair value and not depreciated historical costs. The concept of "goodwill", while used in accounting for commercial transactions has merit, we do not believe that it has merit when accounting in a public sector environment.

6. In your view, should the recipient in an acquisition UCC recognize in its financial statements, on the date of acquisition, the difference arising as:

(a) A gain or loss recognized in surplus or deficit (in the statement of financial performance);
(b) A contribution from owners or distribution to owners recognized directly in net assets/equity (in the statement of financial position); or
(c) A gain or loss recognized directly in net assets/equity (in the statement of financial position), except where the transferor is the ultimate controlling entity and then the gain or loss meets the definition of a contribution from owners or distribution to owners?

Please explain why you support (a), (b), or (c).

FMSB Response: The FMSB supports option (b). The approach suggested by the IPSASB for these transactions is to use the carrying values as the measurement basis for the transactions. We believe that as carrying values may or may not reflect fair value, it would be inappropriate to recognize either a gain or a loss on such transactions. Therefore, approach (b) should be used.

7. In your view, should the accounting treatment for the recipient and transferor of an acquisition UCC be symmetrical?

FMSB Response: The FMSB believes that the accounting for the recipient and the transferor should be symmetrical.

We would like to thank you for allowing us to submit our comments to the exposure draft. Should there be any questions regarding our comments, please contact Steven Sossei at ssossei@agacgfm.org.

Sincerely,

Eric S. Berman, CPA, Chair
AGA Financial Management Standards Board

cc: Evelyn A. Brown, CGFM-Retired
AGA National President