IPSASB

STAFF QUESTIONS AND ANSWERS

May 2018

State-Owned Enterprises and IPSAS-Based Consolidated Financial Statements

Staff of the International Public Sector Accounting Standards Board® (IPSASB®) have issued this Questions & Answers (Q&A) publication to discuss the compatibility for consolidation purposes of IPSAS and accounting frameworks for public sector entities of a commercial nature with profit-seeking objectives. Such entities are known by various terms, including state-owned enterprises (SoEs) and government business enterprises (GBEs), the term used in IPSAS until recently. In this publication, the term SoEs is used to describe such entities, unless the reference is to a previous or current requirement or guidance in IPSAS. SoEs are also known as public corporations in Government Finance Statistics (GFS).

"This document considers the compatibility of IPSAS and accounting frameworks based directly or indirectly on IFRS for consolidation of SoEs."

This publication does not constitute an authoritative pronouncement of the IPSASB or an interpretation of one or more authoritative pronouncements of the IPSASB. It does not amend nor override the requirements of existing IPSAS or provide further implementation guidance. This publication is not meant to be exhaustive and this Q&A is not a substitute for reading the relevant International Public Sector Accounting Standards (IPSAS).

Background

In some jurisdictions where entities are considering IPSAS adoption or are implementing IPSAS, questions arise about the compatibility of IPSAS and the accounting frameworks used for SoEs in the preparation of public sector consolidated financial statements.

This Q&A focuses on compatibility between IPSAS and International Financial Reporting Standards (IFRS), which are developed and maintained by the International Accounting Standards Board, as well as national financial reporting standards that very closely approximate IFRS. Where a SoE applies national financial reporting standards that differ significantly from IFRS, a lack of uniformity of accounting policies may be unavoidable and the controlling entity will need to make a number of conforming adjustments. Paragraph 41 of IPSAS 35, *Consolidated Financial Statements*, discusses circumstances where a member of the economic entity uses accounting policies other than those adopted in the consolidated financial statements.

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Q1. *How does IPSASB communicate the entities for which it is developing IPSAS?*

In *The Preface to IPSAS* the IPSASB states clearly the characteristics of entities for which it is developing IPSAS:

"The IPSAS are designed to apply to public sector entities[1] *that meet all the following criteria:*

(a) Are responsible for the delivery of services[2] *to benefit the public and/or to redistribute income and wealth;*

(b) Mainly finance their activities, directly or indirectly, by means of taxes and/or transfers from other levels of government, social contributions, debt or fees; and

(c) Do not have a primary objective to make profits."

However, the IPSASB cannot mandate which entities adopt IPSAS. This is a decision for the regulator in each jurisdiction. Depending on jurisdictional decisions SoEs will likely either report in accordance with IFRS or other nationally developed financial reporting standards for profit-seeking entities.

Until 2016, most IPSAS included an explicit statement that GBEs report in accordance with IFRS. IPSAS 1, *Presentation of Financial Statements*, included a formal definition of, and guidance on, a GBE, which was repeated widely in the IPSASB's literature. However, this approach was at times confusing, given the other definitions in use for such bodies and the fact that the accounting framework applied by SoEs is a jurisdictional decision.

In 2016 the IPSASB therefore revised the way it communicates the entities for which IPSAS are designed to apply, and removed the definition of a GBE and accompanying guidance. The IPSASB develops accrual-based IPSAS in two different, but complementary, ways:

- By addressing public sector financial reporting issues

  (a) That have not been comprehensively or appropriately dealt with in existing IFRS, or

  (b) For which there is no related IFRS; or

- By developing IPSAS that are converged with IFRS by adapting them to the public sector context.

For example IPSAS 23, *Revenue from Non-exchange Transactions (Taxes and Transfers*), deals with public sector specific transactions such as taxation revenues and inter-governmental transfers. It does not have an IFRS equivalent. Conversely, IPSAS 17*, Property, Plant and Equipment,* is based closely on IAS 16, *Property, Plant and Equipment*, although it does differ in its treatment of revaluation surpluses and deficits.

In order to ensure that public sector specific transactions are appropriately identified when developing standards primarily drawn from an existing and relevant IFRS, the IPSASB has a transparent process. The process is documented in *Process for Reviewing and Modifying IASB Documents,* which is available on the IPSASB website, and is also known colloquially as the "*The Rules of the Road"*. *The Rules of the Road* provides a framework for ensuring that the requirements in IFRS are

[1] Paragraph 1.8 of *The Conceptual Framework for General Purpose Financial Reporting by Public Sector Entities* identifies a wide range of public sector entities for which IPSASs are designed.

[2] Services encompasses goods, services, policy advice and services provided to other public sector entities.

only modified when there is a specific public sector transaction that requires an approach that meets the needs of the users of financial statements, as well as the qualitative characteristics of financial reporting.

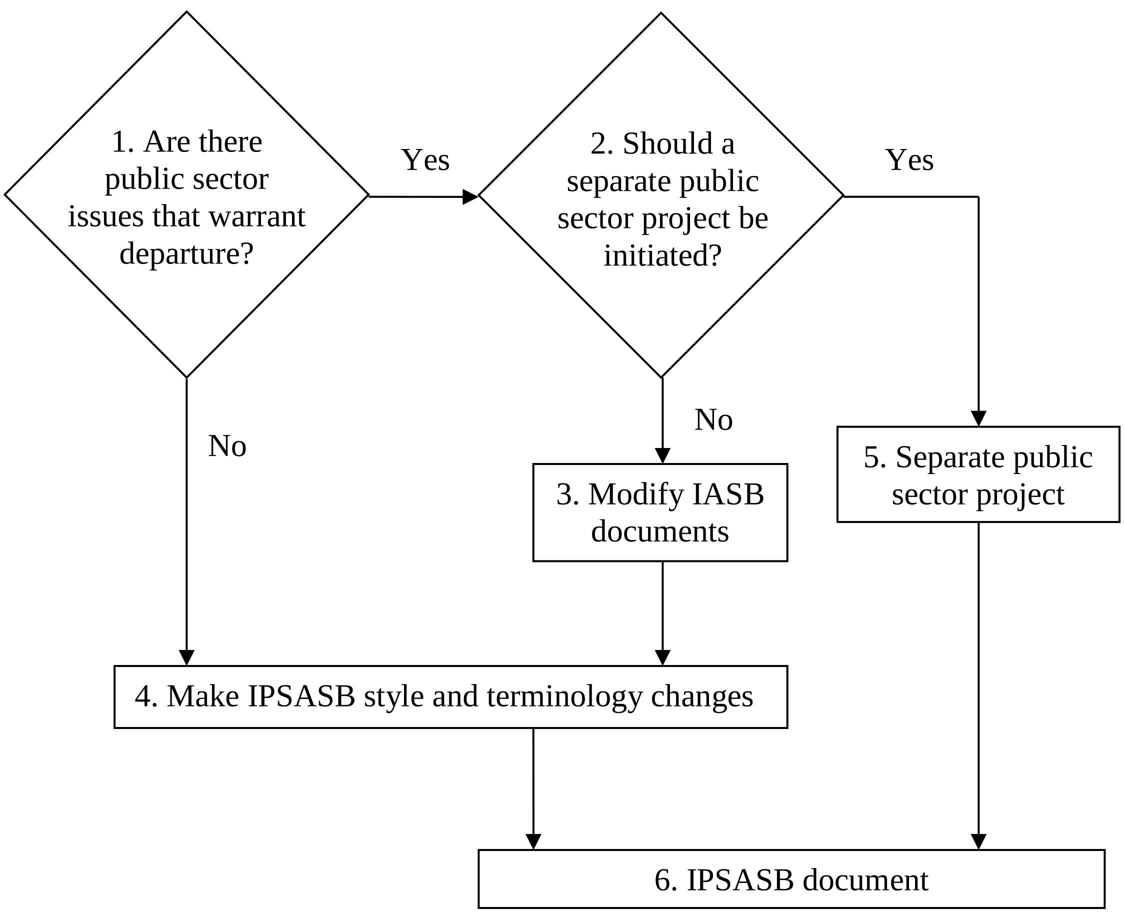
The Rules of the Road also acknowledges departures from IFRS for:

- Consistency with the IPSASB's Conceptual Framework;
- Internal consistency with other IPSAS;
- Consistency with the statistical bases of accounting, principally Government Finance Statistics; and
- Cost-benefit.

The Rules of the Road process therefore limits differences between IPSAS-based and IFRS-based financial statements for consolidation purposes, and enhances the likelihood that the same requirements are applied to a transaction or balance no matter which reporting framework is used.

The main features of the *Rules of the Road* process are set out in the following diagram:

Development of IPSAS - Process for Reviewing and Modifying IASB Documents



Any departures from IFRS in IPSAS developed since 2010 are explained in the Basis for Conclusions in each IPSAS.

Q2. Are there choices of accounting policy in IPSAS?

Yes, a number of IPSAS provide choices of accounting policy in the same way as their equivalent IFRS. For example, IPSAS 17, like IAS 16, permits either the cost model or revaluation model to be used for measurement subsequent to initial recognition. IPSAS 16, *Investment Property*, has a similar accounting policy choice, which reflects IAS 40, *Investment Property*.

IPSASB staff acknowledge that there are some limited differences between IPSAS and equivalent IFRS. Owing to the complexities of the administration of central government borrowing and the difficulty in many cases of attributing borrowing costs to specific capital projects in the public sector, IPSAS 5, *Borrowing Costs*, includes both an expensing and a capitalization option, unlike IAS 23, *Borrowing Costs*, from which it is primarily drawn. IAS 23 requires the capitalization of borrowing costs. The IPSASB's project on Measurement is currently reconsidering this issue.

In early 2018, the IPSASB issued ED 64, *Leases*. For both operational and conceptual reasons, the IPSASB proposes the same accounting model for both lessors and lessees, rather than the lessor accounting model in IFRS 16, *Leases*. Nevertheless, IPSASB staff are of the view that throughout the IPSASB's literature, significant substantive differences between IPSAS and IFRS are fairly limited.

Q3. What can controlling entities do to make consolidation as straightforward and resource efficient as possible?

Central guidance is key to enhancing adoption of consistent accounting policies within a reporting entry by all controlled entities. The provision of central guidance increases the likelihood that the accounting treatments for specific transactions and balances are the same for consolidation purposes. This process is analogous to that applied by the parent company (or 'head office') in the corporate sector, in order to ensure consistency of accounting policies across a group of companies.

An alternative approach is that entities prepare their own individual accounts using the accounting policy of their choice and then supply information to the controlling entity on a comparable (centrally agreed) accounting policy basis for consolidation purposes, making adjustments for differences in treatment where necessary. This approach is used in some jurisdictions for SoEs. However, it is likely to be much more resource-intensive than adopting consistent accounting policies to the extent feasible. IPSASB staff therefore think that this is a sub-optimal approach.

Conclusion

IPSASB staff consider that the use of IPSAS for non-profit-seeking entities should not give rise to significant compatibility issues when SoEs reporting under IFRS, or a similar national framework, are consolidated into a government's financial statements. Provided that the same accounting policies are adopted where there are the same or similar choices under IPSAS and IFRS, the preparation of consolidated accounts should not present significant problems.

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