Proposed International Public Sector Accounting Standard - Consolidated Financial Statements
Comments of Ichabod's Industries on ED 49

Ichabod's Industries is an accountancy consulting firm that provides technical accounting support to a number of local government bodies in the United Kingdom. We have recently been commissioned by the Chartered Institute of Public Finance and Accountancy to draft guidance for their consideration on the application of IFRS 10 by UK local authorities.

We wish to contribute to discussion on Specific Matter for Comment 1 – "Do you agree with the proposed definition of control? If not, how would you change the definition?"

Following the work that we have done to date on the application of IFRS 10 to the public services, we are not convinced that ED 49 is successful in the use of "benefits" instead of "returns" in its definition of control. The reason given on page 62 is that "benefits" gives a better emphasis that returns might be non-financial.

The immediate point to make is that "benefits" reduces the emphasis in IFRS 10 that returns can be positive or negative.

But more widely, the wish to focus on non-financial benefits is questionable when there is no current proposal to seek to quantify non-financial benefits in the consolidated statements that would be prepared to include a controlled entity. Until such time as the consolidation process is developed to properly reflect the non-financial benefits accruing to a parent entity and the risks relating to securing those benefits, then it is arguable that the factors determining whether consolidated accounts are prepared should be restricted to financial returns.

Otherwise there is a possibility that an entity might determine that it gets significant benefits from its involvement with another entity and must include the other entity in its consolidated accounts, but finds that the accounts of the other entity do not include any effective representation of the benefits, their content being restricted to the other entity's returns. The parent would be purporting that its control over the subsidiary is significant but the consolidated accounts would contradict this.

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The change in emphasis raises a potential for many interpretative complications that will only be fully understood when the IPSAS comes to be applied in practice. However, the impact is visible in problems arising directly from one of the paragraphs in the ED. Paragraph 24 looks to settle situations where two entities are competing for control over another entity – ie, they both control relevant activities that significantly affect the returns/benefits they get from another body.

Paragraph 13 of IFRS 10 resolves conflicts by giving predominance to the entity that directs the activities that most significantly affect the returns of the subsidiary entity. This provides a definitive solution in that it focuses on the returns from the perspective of the subsidiary entity, such that there is an pool of returns recognisable for that entity and it can be determined which superior entity takes the greater share of an identifiable whole (eg, of accumulated profits or the residual value of net assets).

The parallel provision in paragraph 24 of the ED looks instead at "the benefits from that entity". This is a much wider field of consideration, bringing in things that might be regarded as benefits for the superior entities in terms of their service objectives that might not actually be intrinsic to the subsidiary entity. For example, an entity might have been formed by a housing provider and a social care provider. The objectives of the former are to make social housing available and is able to direct the entity in its housebuilding programme. The latter's objectives are to house vulnerable persons and is able to direct the entity decisions about occupancy of the properties. Each of the superior entities might be justified in claiming a subsidiary under paragraph 24.

Without a foundation in the subsidiary entity's activity, it may be possible for superior entities to conclude objectively that their own benefits are the most significant and that they have control. They would be required to judge their involvement on their own subjective terms and situations could arise where one entity is consolidated twice or more by superior entities.

Paragraph 24 therefore needs significant reworking because either:

- it is redundant, because the IPSASB takes the view that any entity could be consolidated by multiple parents and the exclusivity provisions of paragraph 13 of IFRS 10 do not need to be replicated in the planned IPSAS – in which case the paragraph can be deleted

  or

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- it cannot be guaranteed to achieve an objective of exclusivity in all situations that will have the same effect as paragraph 13 because of the significant differences between "benefits from an entity" and "returns of an entity" in their ability to set a single measurable quantum for assessing control – in which case a new formulation will be needed to allow competing entities to assess which one has the greatest claim to being the parent.

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