

Ms Stephenie Fox  
The Technical Director  
International Public Sector Accounting Standards Board  
International Federation of Accountants  
529 Fifth Avenue, 6th Floor  
New York, NY 10017 United States of America

Dear Ms Fox

**ED 48, 49, 50, 51 & 52 – EDs on reporting on interests in controlled entities, associates and joint arrangements**

The Heads of Treasuries Accounting and Reporting Advisory Committee (HoTARAC) welcomes the opportunity to provide comments to the International Public Sector Accounting Standards Board (IPSASB) on the Exposure Drafts: ED 48 *Separate Financial Statements* (ED 48), ED 49 *Consolidated Financial Statements* (ED 49), ED 50 *Investments in Associates and Joint Ventures* (ED 50), ED 51 *Joint Arrangements* (ED 51) and ED 52 *Disclosure of Interests in Other Entities* (ED 52).

HoTARAC is an intergovernmental committee that advises Australian Heads of Treasuries on accounting and reporting issues. The Committee comprises the senior accounting policy representatives from all Australian States, Territories and the Australian Government.

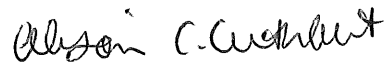
HoTARAC commends the IPSASB's efforts in developing International Public Sector Accounting Standards (IPSASs) for reporting on interests in other entities, specifically controlled entities, associates and joint arrangements. HoTARAC strongly supports the strategy to converge IPSASs with the International Financial Reporting Standards (IFRSs) issued by the International Accounting Standards Board (IASB) and acknowledges the need to consider issues that are specific and unique to the public sector. However, HoTARAC has concerns on some of the proposed accounting treatments that in our view would significantly depart from the IFRS requirements without achieving significant improvements in financial reporting for public sector entities.

In particular, HoTARAC does not support the proposed requirement in ED 49 for extending the consolidation relief to a controlling entity that is not itself an investment entity (that relief proposing that such a controlling entity would measure its investments held by a controlled investment entity at fair value).

The Attachment to this letter sets out HoTARAC's views on those EDs.

If you have any queries regarding HoTARAC's comments, please contact Alison Cuthbert from Queensland Treasury and Trade on 61 7 3035 1431 or by email to [alison.cuthbert@treasury.qld.gov.au](mailto:alison.cuthbert@treasury.qld.gov.au).

Yours sincerely



On behalf of  
**HEADS OF TREASURIES ACCOUNTING AND REPORTING ADVISORY  
COMMITTEE**

20 February 2014

## ATTACHMENT

### HoTARAC RESPONSE TO IPSASB EXPOSURE DRAFTS

*48 SEPARATE FINANCIAL STATEMENTS*

*49 CONSOLIDATED FINANCIAL STATEMENTS*

*50 INVESTMENTS IN ASSOCIATES AND JOINT VENTURES*

*51 JOINT ARRANGEMENTS*

*52 DISCLOSURE OF INTERESTS IN OTHER ENTITIES*

#### **General comments**

HoTARAC strongly supports the IPSASB's strategy to converge IPSASs with IFRSs in developing accounting standards for public sector entities and to only consider modifications for unique issues that are specific to the public sector.

While HoTARAC agrees on most of the proposals in the EDs, HoTARAC has some concerns about the proposed accounting treatments that in our view would significantly depart from the IFRS requirements without achieving significant improvements in financial reporting by public sector entities.

In particular, HoTARAC does not support the proposed requirement in ED 49 requiring a controlling entity that is not itself an investment entity to account for its investments held by a controlled investment entity at fair value through profit or loss. In most other instances, HoTARAC considers that the proposed additional or alternative requirements are unnecessary and/or potentially confusing.

The following comments set out HoTARAC's detailed responses on those EDs. Given HoTARAC only has a limited number of concerns, comments contained in this attachment do not address each Specific Matter for Comment outlined in each of the EDs.

**ED 48 - 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?*

HoTARAC notes that the IPSASB has added an option allowing the use of the equity method in separate financial statements. HoTARAC generally agrees with the IPSASB's view that as well as the existing cost and fair value options, the equity method could also be used to faithfully reflect the underlying circumstances of certain investments held by public sector entities. As a related note, HoTARAC notes the IASB has also issued an ED that proposes to restore the equity method option to account for investments in subsidiaries, joint ventures and associates in an entity's separate financial statements. Subject to the final IASB determination, HoTARAC supports the proposal to permit, but not require, the use of the equity method in separate financial statements for investments in other entities.

**Editorial suggestions**

**ED 48 – paragraph 19**

Given paragraph 21 also discusses relevant disclosure requirements for an investment entity that prepares separate financial statements, HoTARAC believes that paragraph 19 should refer to '*requirements in paragraph 20 ~~and~~ to 22*'.

**ED 49 - Specific Matters 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 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 of 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?*

HoTARAC notes that the proposed requirement in paragraph 54 of the ED is inconsistent with IFRS requirements where only a parent that meets the definition of investment entity is allowed to account for their investments at fair value through profit or loss. HoTARAC is not convinced that there is a specific public sector reason to diverge from IFRS requirements and does not consider this modification as proposed by the IPSASB is appropriate.

HoTARAC agrees that the structure of an entity should not dictate the accounting and acknowledges the importance of consistency in application of accounting treatments, where achievable, at different consolidation levels. However, HoTARAC believes that in practice, consolidation exemptions should only be allowed in limited circumstances (e.g. when the controlling entity itself meets the definition of an investment entity). In most other situations when an entity controls another entity, it should consolidate it.

The above HoTARAC view is supported by the following points:

- Consistent with HoTARAC's submission on the IASB's ED on *Investment Entities*, HoTARAC believes that excluding non-investment entity parents from accounting for investments held by its investment entity subsidiaries at fair value is essential to help avoid structuring opportunities that might achieve particular accounting outcomes;
- The structuring opportunities (e.g. allocating certain investments to a controlled investment entity), would lead to manipulation of financial statements (by retaining the fair value treatment on consolidation) if the ultimate parent is not itself an investment entity;
- HoTARAC supports the IPSASB's decision to retain the consolidation exemption for investments that are controlled by an investment entity based on the view that consolidation by the investment entity would not

provide decision-useful information. As such, fair value accounting in this instance would better reflect the nature and attributes of the investment entity (i.e. profit-oriented) and investments that it holds. However, given it is highly unlikely that the objective of the ultimate public sector parent (e.g. a State/Provincial government) would be for-profit, HoTARAC questions the appropriateness of extending the consolidation relief to a not-for-profit public sector parent that is not itself an investment entity;

- HoTARAC also believes the proposal to extend the consolidation relief to a not-for-profit public sector parent that is not itself an investment entity, would reduce public sector accountability and transparency by avoiding consolidation of certain assets and liabilities that are controlled by its investment entity subsidiary; and
- The proposal would lead to an unwarranted departure and potentially significant divergence from IFRS requirements.

HoTARAC therefore would urge the IPSASB to reconsider the proposed approach in ED 49, in particular, the appropriateness of extending the consolidation relief to a not-for-profit public sector parent.

Any consequential redeliberation by the IPSASB on this issue would also impact proposed requirements in ED 48 *Separate Financial Statements* (paragraph 14) and ED 52 *Disclosures of Interests in Other Entities* (paragraph 34).

## **Other comments**

### **ED 49 - Use of the term ‘binding arrangement’**

ED 49 introduces the concept of ‘binding arrangements’ to cover situations in which entities applying IPSASs do not have the power to enter contractual arrangements. The definition of paragraph 10 suggests that this is intended to apply to contract-like arrangements and BC43 states that references to ‘contractual arrangements’ in IFRS should be replaced with ‘binding arrangements’. However, paragraph AG20 of ED49 refers to contractual arrangements and rights in considering whether an entity’s appointment rights for key personnel are sufficient to give it control.

The IPSASB have also added paragraph AG38, which refers to the power to appoint a governing body arising from ‘binding arrangements (including existing legislation, regulation, contractual, or other arrangements)’. Example 15 suggests that the power to appoint trustees to a museum satisfies this criterion. In this instance, the term ‘binding arrangement’ seems to be applied more broadly than contract-like arrangements.

The definition of binding arrangements is also included in EDs 50, 51 and 52, but without the explanation in the basis of conclusions, so it is unclear in what context the term is used in these exposure drafts. For example, paragraph 35 of ED 52 refers to a contractual relationship, while binding arrangements are

referred to in the rest of the ED. The term ‘contractually’ is applied in the definition of joint control in ED 50, but joint arrangements in ED 51 is defined in terms of ‘binding arrangements’ in paragraph 10. ED 52 paragraph 30 requires that an investment entity disclose restrictions arising from binding arrangements, while paragraph 32 requires disclosure of contractual arrangements for the provision of financial support.

If the terminology used in these cases is deliberate, additional explanation in the basis for conclusions would be useful to prevent confusion in the application of the requirements and the distinction between ‘contractual’ and ‘binding’ arrangements.

Additionally, given the rationale stated (i.e. that this applies where entities are unable to enter formal contractual relationships), the IPSASB may wish to consider the consistency of this approach with the references to contractual rights and arrangements in other IPSASs, for example, those related to financial instruments.

#### **ED 49 - Example 4**

Although HoTARAC agrees with the conclusion of the example, HoTARAC considers that a government that has the power to impose regulatory control might, arguably, meet the control criteria as such power would significantly influence the returns of the electricity distributor being regulated. This is particularly relevant when the electricity distributor being regulated is a Government Business Enterprise and may, depending on each governmental arrangement, provide dividend payments or dividends-in-kind to the government. More discussions may be needed to better articulate the argument in concluding why the government or the regulator does not control the electricity distributor in the example.

#### **Editorial suggestions**

##### **ED 49 – paragraph 54**

Additional numbering may need to be added to the second last line of the paragraph so that it reads ‘*shall (ii) consolidate the other assets and liabilities and revenue and expenses of the controlled investment entity in accordance with paragraph 34-51 of this standard*’.

##### **ED 49 – paragraph AG 105**

Reference is made to paragraph 50(c) in the context of investment entities, whereas the actual paragraph referred to is about accounting treatment when a controlling entity loses control of an entity.

**ED 49 – Flowchart 2 on page 66**

The box on the right hand side of the flowchart should contain the alternative outcome resulting from the flowchart decision (e.g. entity does not control the other entity).



**ED 50 - 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?*

HoTARAC notes that the existing IPSAS 7 *Investments in Associates* applies when an investor holds an ownership interest in the form of a shareholding or other formal equity structure and the ED intends to provide further clarification about the type of ownership interests that would qualify for equity accounting. Neither IAS 28 *Investments in Associates and Joint Ventures* nor IFRS 11 *Joint Arrangements* contain similar ownership requirements. HoTARAC understands that, in practical terms, it is unlikely that equity accounting would be applied by private sector investors that do not have quantifiable formal ownership interests in associates or joint ventures, this may not necessarily be the case in the public sector.

The subtle difference between IFRSs and revised IPSAS 7 would cause a divergence in practice when applying equity accounting between private and public sector entities. Public sector investors that have investments in associates and/or joint ventures through interests other than formal ownership would be prohibited from using equity accounting. This prohibition does not apply to investors in the private sector.

The IPSASB should clearly explain in the Basis for Conclusions the rationale for scoping out investments that do not involve quantifiable formal ownership interests, and justify whether such a departure is warranted by a situation that is unique to the public sector.

To achieve consistency and minimal departure from IFRSs, HoTARAC suggests that the IPSASB review the existing 'ownership interest' requirement in IPSAS 7 and recommends the IPSASB only modify IFRSs when there are unique public sector specific issues that would warrant such modification.

**Editorial suggestions**

**ED 50 – paragraph 30**

The cross-references mentioned at the end of the paragraph may be more appropriate to refer to paragraphs 37 and 38 (instead of paragraphs 36 and 37).

**ED 50 – paragraph 33**

The reference to paragraph 30 may more appropriately be changed to paragraph 31.

**Other comments**

**ED 51 – Example 3 variation – Joint Provision of Assisted Living Services**

IE18 in example 3 specifies that entity X will be responsible for providing the assisted living services and entity Y will be responsible for the construction and ongoing maintenance of the premises. IE20 states that entity X and Y should recognise their share of the revenue and expenses resulting from the provision of assisted living services through the new entity Z.

Given entity Y will not be directly involved in providing the assisted living services, IE20 appears to suggest that the proposed basis for allocating revenue and expenses would only be applicable to entity X but not entity Y. HoTARAC suggests that the IPSASB review the proposed allocation basis in the example, to ensure it is consistent with the surrounding paragraphs.

**ED 52 - 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.*

Although HoTARAC acknowledges that a public sector structured entity may involve other rights other than voting rights, the proposed definition is cumbersome and potentially confusing.

HoTARAC agrees with the IPSASB's analysis that 'similar rights' in the IASB's definition of a 'structured entity' would encompass broader rights. Arguably such rights would also capture administrative arrangements and statutory provisions. To avoid unnecessary departure from IFRS requirements and prevent potential misinterpretation of the proposed definition, HoTARAC recommends the IPSASB only address this issue in the application guidance as currently presented in AG20 while retaining the IFRS definition of 'structured entity' without amendment.

**Other comments**

**ED 52 – paragraph 23**

HoTARAC notes that paragraph 23 does not exactly replicate the wording of the corresponding IFRS paragraph and the IPSASB's wording '*previously met the definition of a structured entity and was not consolidated*' could be read to imply that after a controlling entity obtained control over a structured entity, the structured entity would no longer meet the definition of a 'structured entity'. HoTARAC suggests that the IPSASB clarify this wording, as a structured entity could continue to meet the 'structured entity' definition, even after it becomes controlled.