

Meeting: International Federation of Accountants
Board

Meeting Location: Brussels, Belgium

Meeting Date: September 15-18, 2014

Agenda Item 8

For:

☐ Approval

☒ Discussion

☐ Information

Issues Paper, *Public Sector Combinations*

Objective(s) of Agenda Item

1. The objective of this session is to **review** an Issues Paper on Public Sector Combinations; and to **provide directions** on the classification of public sector combinations.

Material(s) Presented

Agenda Item 8.1 Issues Paper, *Public Sector Combinations*

2. The detailed analyses of the responses to the Preliminary Views and the Specific Matters for Comment were presented at the June 2014 meeting and are not duplicated in this agenda item. Members wishing to review the analyses are referred to the June 2014 meeting papers.

Action(s) Requested

3. The IPSASB is asked to consider the issues raised in the Issues Paper and to:
 - (a) Agree that the same accounting treatment should be applied to all combinations UCC;
 - (b) Provide direction as to the classification of combinations NUCC; and
 - (c) Confirm that the formation of joint ventures is outside the scope of the project.

Issues Paper, *Public Sector Combinations*

Introduction

1. As noted in the Issues Paper presented at the June 2014 meeting, Exposure Draft (ED) 41 *Entity Combinations from Exchange Transactions*, was issued in May 2009. After considering the comments received the IPSASB decided to undertake a broader scope project that considered all combinations in the public sector. The IPSASB issued the Consultation Paper (CP) *Public Sector Combinations* in June 2012.
2. Staff presented a detailed review of responses to the CP to the June 2014 IPSASB meeting and proposed an approach to classification that used ownership to supplement control. After some discussion the IPSASB decided not to adopt this approach and directed staff to further develop options for classification based on the approach in the Consultation Paper. These options are to take into account the suggestions made by respondents, including whether there is consideration and whether a combination is an exchange transaction. The IPSASB agreed that decisions on measurement and transferor accounting would be deferred until the approach to classification has been agreed.
3. This Issues Paper considers the classification of public sector combinations, starting with the approach outlined in the CP. It then discusses the suggestions made by respondents to the CP and identifies and considers the merit of approaches proposed by respondents.

Consultation Paper Proposals for Classification

4. The CP proposes a number of definitions, of which the following are relevant to this issues paper:

A **public sector combination** is the bringing together of separate operations into one entity, either as an acquisition or an amalgamation. (PV1)

An **acquisition** is a transaction or other event that results in a recipient gaining control of one or more operations. (PV1)

An **amalgamation** is 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. (PV1)

A **public sector combination under common control** is a public sector combination in which all of the entities or operations involved are ultimately controlled by the same entity both before and after the public sector combination. (PV 2)
5. The CP proposes that combinations should be distinguished initially between acquisitions and amalgamations and that:
 - For amalgamations, the modified pooling of interests method of accounting be applied.
 - For acquisitions UCC, the recipient recognizes the assets acquired and the liabilities assumed at carrying amount.

6. For acquisitions, NUCC, the CP seeks views on whether the recipient should recognize assets and liabilities acquired:
 - At fair value for all acquisitions; or
 - At fair value for those acquisitions which involve consideration. Carrying amount would be adopted where the acquisition involved no or nominal consideration.
7. The CP proposes that where the net assets acquired exceed the consideration transferred the recipient recognizes a gain in surplus and deficit and, where the recipient assumes net liabilities of the transferred operation, a loss. The CP does not reach a conclusion on whether goodwill or a loss should be recognized where the recipient transfers consideration exceeding the net assets acquired.
8. Staff notes that the CP proposes measuring some combinations at fair value. This is consistent with the approach in IFRS 3. Staff also notes that the draft Conceptual Framework does not include fair value as a measurement basis. Whilst this Issues Paper refers to fair value for consistency with the CP, the ED to be developed at a later stage will propose measurement bases adopted in the Conceptual Framework.

Responses to the Consultation Paper - Classification

9. Twenty-six respondents commented on the CP. There is a diversity of views amongst respondents. However, the responses contain common themes irrespective of whether a respondent supports the classification basis proposed in the CP or not. Respondents 1, 3, 5, 7, 8, 10, 11, 12, 14, 15, 17, 20, 22, 23, 25, and 26 raised concerns in relation to distinguishing between an acquisition and an amalgamation. Respondents 4, and 10 explained that additional guidance on assessing whether an entity had gained control is required.
10. Respondent 20 commented: "We agree with the preliminary views in the CP. However, we recognize the challenge of developing practical guidance to help determine whether a combining operation gains control of the other operation(s) in [a combination] of operations of different sizes."
11. Respondent 22 commented: "Definitions appear reasonable although further clarification is required to identify the circumstances whereby amalgamation not under common control might happen".
12. For respondents 7 and 23, the definitions in the CP do not adequately differentiate between an acquisition and an amalgamation.
13. Respondent 23 commented: "The [respondent] is of the view that this definition [of an amalgamation] is too narrow and therefore does not encompass the range of possible combinations that would fall into the realm of an amalgamation (i.e., combinations that are not an acquisition). The Board considers that more emphasis should be put on the outcome of a combination, rather than on the process, which appears to be the main focus of the CP. To this end a future ED should be drafted in two separate sections, one addressing pure acquisitions and the other addressing amalgamations or reorganizations."
14. Respondent 7 also considered that the examples in the CP did not explain how to apply the definitions to determine the substance of a combination: "The examples given in Chapter 2 (as set out in diagrams 1, 2 and 3) of acquisitions and amalgamations appear to be based on legal form. In contrast, if the combining operations maintain their separate legal structure (as in diagrams 1 and 2) it appears that the combination is viewed as an acquisition. But if the two operations are combined to create a single legal entity (as in diagram 3 and discussed in paragraphs 2.39 and 2.40), it is viewed as an

amalgamation. Given the definition of a public sector combination is “the bringing together of separate operations into one entity, either as an acquisition or an amalgamation”, it’s not clear why the legal form is so important”.

15. These concerns over the precise boundary between an acquisition and an amalgamation has led to a variety of responses, from requests for additional guidance to proposals for an alternative approach to classifying combinations. These are discussed later in this Issues Paper.
16. The distinction between combinations UCC and those NUCC does not generate the same level of uncertainty. Respondents do not express any uncertainty as to where the boundary lies. Respondent 23 considers this distinction should be the primary distinction.
17. Respondents noted that determining whether an entity is a controlled entity is not always straightforward. This is not an issue for this project, and is addressed in the project on interests in other entities. It is, however, a factor in determining whether a combination occurs UCC.
18. A list of respondents is provided at Appendix A to this Issues Paper.

Proposed Classification Approach

Combinations NUCC and Combinations UCC

19. The analysis of public sector combinations in the CP takes the distinction between acquisitions and amalgamations as the starting point. Staff considers that the distinction between combinations NUCC and those UCC is the most appropriate primary distinction.
20. The CP proposes measuring both acquisitions UCC and amalgamations UCC at carrying amount; the accounting treatment is therefore likely to be the same for all combinations UCC. Staff proposes that the pooling of interests method is adopted for all combinations UCC, for the following reasons:
21. When a combination takes place UCC, the ultimate controlling entity can determine the terms of the combination. This includes whether consideration is transferred, and if so how much. It also includes the form of the transfer, including whether one entity gains control of the transferred operations or not. Requiring different accounting treatments of combinations UCC depending on whether the combination met the definition of an acquisition or an amalgamation may not reflect the economic substance of the transaction. It may also provide opportunities for “gaming”, with the ultimate controlling entity being able to modify the terms of the combination to achieve a desired financial reporting outcome.
22. IFRS 3 defines goodwill as “an asset representing the future economic benefits arising from other assets acquired in a business combination that are not individually identified and separately recognized.” Where the ultimate controlling entity can determine the terms of the combination, including the consideration transferred, the difference between the consideration paid and the fair value of the net assets acquired may not faithfully represent future economic benefits. Acquisition accounting may, therefore, not meet the objectives of financial reporting for combinations UCC.
23. A combination UCC does not result in changes to the resources controlled, obligations incurred or financial performance of the ultimate controlling entity, or the financial statements of the ultimate controlling entity that present such information. The ultimate controlling entity may determine the accounting policies used in the preparation of a controlled entity's financial statements. These financial statements will meet the objectives of financial reporting. It is therefore expected that

measuring a combination UCC at carrying amount will also meet the objectives of financial reporting. For this reason, the additional information provided by restating assets and liabilities at fair value may not justify the cost involved.

24. Combinations UCC frequently occur when government ministries or agencies are reorganized. Citizens will often hold the Government as a whole accountable for the performance of these ministries or agencies. As a combination UCC may result in no change in accountability in these circumstances, measuring the combination at carrying amount would provide information that was useful for accountability purposes.

Matter(s) for Consideration

1. The IPSASB is asked **to indicate** whether it supports the staff recommendations that:
 - (a) The primary distinction should be between combinations UCC and combinations NUCC;
 - (b) That combinations UCC should form a single classification incorporating the acquisitions UCC and amalgamations UCC classifications identified in the CP; and
 - (c) That combinations UCC should be measured at carrying amount and accounted for using the pooling of interests method.

Acquisitions and Amalgamations NUCC

25. As seen in the previous paragraphs, this Issues Paper proposes that the same accounting treatment be used for all combinations UCC. The discussion of the boundary between acquisitions and amalgamations in the remainder of this Issues Paper therefore concentrates on combinations NUCC. The IPSASB may decide not to apply the same accounting treatment to all combinations UCC. Should this be the case, most (but not all) of the issues raised in respect of combinations NUCC are expected to apply equally to combinations UCC.
26. Although the CP provides examples of acquisitions and amalgamations, respondents 7 and 23 find these difficult to interpret. Respondents comment that the examples appeared to be based on the legal form of the combination rather than the substance of the combination.
27. Respondents 7 and 23 find the combination of two public sector entities NUCC difficult to interpret. A combination of municipalities is a typical example of such a combination in most jurisdictions. The legal form of this combination could be either the creation of a new legal entity, or the retention of the legal form of one of the entities for the new, combined entity, with the other entity being wound up.
28. In the second case, the legal form of the combination would meet the definition of an acquisition. However, some respondents comment that the outcome of the combination would be the same irrespective of the legal form. Respondent 7 gives other examples.
29. These concerns led staff to conclude that the definitions in the CP need to be supplemented by guidance on how to determine whether an entity has gained control of another operation or entity through a public sector combination. Staff has therefore taken the CP as the starting point and considered whether any of the factors identified by respondents and by staff could form the basis of such guidance.

Combination of factors

30. Staff has concluded that some factors provide useful guidance when determining whether an entity has gained control of another operation or entity through a public sector combination. Staff has also concluded that no factor provides definitive guidance, and that factors may be more significant in some jurisdictions than others. Professional judgment will be required when applying the factors.
31. Respondents 16, 23 and 24 considered that all factors should be taken into account in determining whether a combination was an acquisition or an amalgamation. For example, respondent 23 “does not agree that the sole definitive criterion for distinguishing an amalgamation from an acquisition should be that none of the combining operations gains control of the other operations. Although gaining control is a necessary condition for an acquisition to occur, it is not of itself sufficient. All facts and circumstances need to be considered together with the substance of the transaction.”
32. Staff proposes to develop an ED using the current definitions of an acquisition and an amalgamation as the basis of classification for combinations NUCC. The ED would include guidance on determining when one entity gains control of an operation or entity. The guidance would discuss those factors that the IPSASB consider relevant to distinguishing between an acquisition and an amalgamation.
33. Staff has considered the following matters. These are discussed in more detail below.

Proposed for inclusion in an ED	Not proposed for inclusion in an ED
Transfer of consideration or significant consideration	Political control
Exchange Transactions	Combination occurs at market price
Combination involves a change in sector	Distinguish between acquisitions NUCC and all other combinations
Whether a combination is voluntary or involuntary	Combination has commercial substance
Nature of jurisdiction	The operation of Government, such as legislation, decrees and budget process
	Government has a residual financial interest in the net financial assets of the entity
	An entity is involved in directing public policy and/or engaging in non-market activity mainly financed by public resources

Matter(s) for Consideration

2. The IPSASB is asked **to indicate** whether it agrees with the approach proposed by staff of including guidance on determining when one entity gains control of an operation or entity.

Transfer of consideration or significant consideration.

34. Respondents 1, 15 and 17 suggest that an acquisition would be indicated where a combination involves the transfer of significant consideration. Respondent 20 suggests a similar distinction based on whether or not consideration is exchanged. These respondents consider that this classification would be simpler to apply.
35. This approach is similar to the one set out in GASB Statement No. 69 *Government Combinations and Disposals of Government Operations*, which was issued in January 2013. GASB Statement No. 69 classifies combinations as acquisitions where there is significant consideration. Government acquisitions are measured at acquisition value, a market-based entry price. For combinations that do not involve the exchange of significant consideration, a further distinction is made. The Statement distinguishes between mergers and transfers of operations, based on whether the combination involves legally separate entities. Carrying amount is adopted as the measurement basis in both cases.
36. The transfer of consideration or significant consideration suggests that an exchange transaction has taken place. One entity would be transferring consideration or significant consideration in exchange for gaining control of an operation or entity. Because the transaction results in the entity gaining control of an operation or entity, the combination would satisfy the definition of an acquisition.
37. Staff notes that a number of circumstances may give rise to a combination that does not involve the transfer of consideration or significant consideration. Such circumstances may give rise to either an acquisition or an amalgamation, as shown below:
- This may reflect the fair value of an entity, or one entity may assume the net liabilities of another entity. These scenarios do not preclude an acquisition as defined by the CP.
 - This may indicate that there has been a “bargain purchase.” IFRS 3 includes guidance on this type of transaction, which may also meet the definition of an acquisition. A bargain purchase may be voluntary or take place under compulsion.
 - This may reflect an uncompensated seizure of assets (i.e., a forced nationalization). This is likely to meet the definition of an acquisition.
 - A lack of consideration may reflect the constitution of the jurisdiction rather than the nature of the combination. The constitutional arrangements may be that all combinations of public sector entities (for example, the reorganization of two municipalities) take place without the possibility of consideration being paid, irrespective of the nature of the combination. Such combinations may meet the definition of an acquisition or an amalgamation. In some jurisdictions, similar arrangements apply to the transfer of operations. In other jurisdictions, consideration is payable for the transfer of an operation that is part of an entity.
 - A lack of consideration may also occur in cases of donations. This would meet the definition of an acquisition.
38. Staff considers that the presence of consideration or significant consideration in a combination NUCC is an indicator of an acquisition. The absence of consideration should not be taken as an indication of an amalgamation.
39. SMC 4 in the CP seeks respondents' views on whether different measurement bases should apply to acquisitions NUCC where no or nominal consideration is transferred (carrying amount) and those

where consideration is transferred (fair value). Staff considers that the transfer or otherwise of consideration should be treated as a classification issue, as all transactions in a class should be measured on the same basis. The absence of consideration should be taken into account in determining the classification of the combination.

Combination is an Exchange Transaction

40. Staff suggests that whether a combination is an exchange transaction is a factor in determining whether that combination is an acquisition or an amalgamation.
41. As noted in the CP, "IFRS 3 includes bargain purchases within its scope. Some respondents noted that because of the inclusion of bargain purchases, it could be argued that IFRS 3 also applies to at least some non-exchange entity combinations. These respondents were concerned about the application of the IFRS 3 approach to non-exchange entity combinations. The IPSASB noted these arguments. The IPSASB acknowledged that it may be difficult to establish a clear demarcation between all exchange and non-exchange entity combinations."¹
42. Staff considers that where it is clear that, in the combination, one entity receives assets or services, or has liabilities extinguished, and directly gives approximately equal value to another entity in exchange, this is indicative of an acquisition. Where a combination is a non-exchange transaction, this fact on its own will be inconclusive. It is necessary to consider related factors, such as the sectors in which the entities operate, before coming to a conclusion as to whether this factor provides any guidance as to the nature of the combination.
43. Staff considers that determining whether a combination is an exchange transaction may prove difficult in some cases. Difficulties may arise in classifying combinations where an exchange has taken place, but the value received by an entity does not appear to be approximately equal to the value it has transferred. This may indicate that the transaction is a non-exchange transaction, but it may also indicate a bargain purchase as defined in IFRS 3. A bargain purchase is likely to meet the definition of an acquisition. Although one party appears to have transferred greater value than they have received, it is likely that they consider they have received value in other ways that are not reflected in the fair value of the transaction. For example, an entity may accept a lower price for the transfer of an operation if that transfer can be achieved in a short period of time, permitting the entity to concentrate on its priorities.
44. Staff considers that distinguishing between a non-exchange transaction and a bargain purchase may prove difficult. Staff therefore concludes that whilst consideration of whether a combination is an exchange transaction will help in determining the classification of combinations, it is unlikely to be definitive.

The combination involves a change in sector

45. Respondent 23 considered that combinations involving a public sector operation and a private sector operation were likely to meet the definition of an acquisition
46. Staff considers this to be appropriate. The fact that after the combination, the combined entity is a public sector entity provides evidence that the public sector entity has gained control of the private sector entity.

¹ IPSASB Consultation Paper *Public Sector Combinations*, paragraph 1.7

47. The situation may be less straightforward where minority interests are involved, for example where an entity partially owned a private sector entity and partially owned by a public sector entity combines with another public sector controlled entity. It is possible that after the combination, neither combining entity gains control.
48. Staff therefore considers that where a combination involves a change in sector, this is an indicator that a public sector entity has gained control of the entity, but is not conclusive.

Whether a combination is voluntary or involuntary

49. The CP identifies the fact that many public sector combinations may be imposed by a higher level of government that does not, for financial reporting purposes, control the entities involved in the combination.
50. Respondents 11 and 23 consider that where a combination is imposed by a higher level of government, this is an indicator that the combination is an amalgamation.
51. Where a combination is imposed by a higher level of government, the operations involved in the combination are unable, through their power over the other entity, to affect the nature and amount of the benefits to which they are exposed. The ability to affect the nature and amount of the benefits through the combination rests with the higher level of government.
52. Staff questions whether this approach would give an unambiguous answer in all circumstances. In some jurisdictions, changes to the structure of public sector entities can only occur through a legislative process. In these jurisdictions, entities that elect to combine (and where one entity may have control over another) would require legislation to be enacted to enable the combination to take place. Such combinations would need to be distinguished from those combinations which were imposed by a higher level of government.
53. The distinction between combinations entered into voluntarily and those imposed by a higher level of government may not be obvious where the same legislative process is required in both cases. An example would be where a combination was initiated by a higher level of government and the entities involved agreed to participate. Would such a combination be voluntary or involuntary?
54. In other jurisdictions, public sector entities may be able to combine without the requirement for a legislative basis. Where voluntary combinations take place, it will be necessary to consider other factors to determine whether the combination is an acquisition or an amalgamation.
55. Another example where the involuntary nature of the combination may not be sufficient to classify the combination as an amalgamation is a nationalization. When a government nationalizes a private sector entity, it often does so through legislation. Nationalizations may involve the compulsory transfer of an entity from its private sector owners to the public sector. This is likely to meet the definition of an acquisition because the government is gaining control of the operations.
56. The public sector can also gain control over private sector entities on contractual arrangements on a voluntary basis where the owner of the private sector entity cedes control in exchange of financial assistance without the shares being transferred.
57. Staff has concluded that considering whether a combination has been imposed by a higher level of government may provide useful information about whether an entity is able to exercise control. However, the fact that a combination has been imposed by a higher level of government does not in itself indicate an acquisition nor an amalgamation.

Nature of jurisdiction

58. Staff notes that respondents have different views as to the approach to consolidation that should be adopted and the information that is required for accountability and decision-making purposes. Staff considers that this may reflect the different ways that the public sector may operate in different jurisdictions.
59. One view suggests that all entities operating in the public sector operate as part of a single quasi “group” entity. This view may arise in jurisdictions where there is significant interaction or redistribution between the different levels of government. Because one level of government does not control the other level, they do not form an economic entity as defined in IPSASs. However, combinations of entities within that quasi-group would be seen as analogous to a combination under common control.
60. Under this view, information about the fair value of a combination is seen as less important. The national government or the parliament is held responsible for the operation of the wider system as a whole. A combination is not seen as representing a change in accountability. Service users may expect the services they receive to be unaffected by the combination, as any reduction in the net assets of the entities providing those services would be compensated through redistribution arrangements. Measuring a combination at carrying amount would meet the information needs of users. The additional information provided by measuring a combination at fair value would not justify the additional cost associated with remeasuring assets and liabilities.
61. In other jurisdictions where there is less interaction or redistribution between the different levels of government, public sector entities are not considered as part of an overall system, but as independent organizations. In these circumstances, entities are not part of a quasi-group, and combinations are not analogous to a combination under common control.
62. Under this view, a combination is seen as directly impacting the services users receive and the resources they provide. Users of financial statements will seek information to assess accountability at a local level, and may see combinations affecting this accountability. Information about the fair value of a combination will enable them to assess the likely impact on future services and taxation. Measuring the combination at fair value is likely to meet the information needs of service users.
63. Staff notes that these examples may represent the two ends of the spectrum. Other jurisdictions may operate between these end points.
64. Staff considers that the nature of the jurisdiction and the operation of the public sector is a factor that may provide useful information in determining whether an entity has gained control of another operation or entity.
65. In jurisdictions where there are significant collaborative arrangements, a combination of two entities may be more likely to be an extension of those collaborative arrangements. This would suggest a combination is more likely to be an amalgamation. Conversely, in jurisdictions where collaborative arrangements are rare, acquisitions may be more likely.
66. Staff considers that no universal conclusions can be drawn from the operation of the public sector in a specific jurisdiction, but that considering this factor can provide useful information about the context in which a combination has taken place. It therefore provides useful information about whether an entity has gained control of an operation or entity.

Matter(s) for Consideration

3. The IPSASB is asked **to indicate** whether it agrees with the staff conclusions that:
- (a) The presence of consideration or significant consideration in a combination is an indicator of an acquisition;
 - (b) The absence of consideration should not be taken as an indication of an amalgamation, but should be considered when classifying of the combination;
 - (c) Where a combination is clearly an exchange transaction, this is an indicator of an acquisition;
 - (d) Where a combination is clearly a non-exchange transaction, this is not an indicator of an amalgamation;
 - (e) Where distinguishing between a non-exchange transaction and a bargain purchase difficult, consideration of whether the combination is a non-exchange transaction is likely to be informative but inconclusive;
 - (f) A change in sector is an indicator that a public sector entity has gained control in a combination, but is not conclusive;
 - (g) Where a combination has been imposed by a higher level of government, this may provide useful information about whether an entity is able to exercise control, but does not in itself indicate an acquisition nor an amalgamation; and
 - (h) Considering the operation of the public sector in a specific jurisdiction provides useful information about the context in which a combination has taken place.

67. Staff considered a number of other factors identified by respondents or by staff, and concluded that these do not provide information that is useful in determining whether a combination is an acquisition or an amalgamation. These are discussed in the following paragraphs.

Political control

68. The CP considered the characteristics of an amalgamation identified in IAS 22, *Business Combinations*. Staff has considered whether the analysis of shareholders' voting rights in IAS 22 could be replaced by political control. IAS 22 refers to voting rights. In some public sector entities, including many municipalities, voting rights will be held by elected politicians.
69. In some jurisdictions, a combination of two municipalities will be accompanied by elections to the new municipality. Whether one group of elected politicians gains control will therefore depend on the electorate. Where new elections are not held, whether one group of politicians has the possibility of gaining control will depend on the political make-up of the municipalities involved. This is particularly the case where local politicians belong to different political parties.
70. In some jurisdictions, elected politicians may belong to a single party, or may not belong to any party. In other jurisdictions, politicians may not be elected but may be appointed. Political control may therefore be difficult to establish.
71. Elected or appointed politicians can be seen as analogous to a company board. Changes to the board does not provide information as to whether a company has gained control of an operation or

an entity. Staff therefore considers that political control is unlikely to be relevant in identifying an amalgamation in a public sector combination.

Combination occurs at market price

72. In replying to SMC 2, respondent 3 distinguishes between acquisitions at market price and all other combinations, which are to be classified as amalgamations.
73. Staff is unsure as to whether the respondent is proposing market price as an alternative classification basis to control, or suggesting that an entity only gains control of an operation or entity if the combination occurs at market price.
74. If the respondent is proposing market price as an alternative classification basis to control, staff considers that this is contrary to the direction given by the IPSASB at the June 2014 meeting. At that meeting, the IPSASB requested staff to develop the classification of public sector combinations based on the proposals in the CP.
75. If the respondent is suggesting that an entity only gains control of an operation or entity if the combination occurs at market price, staff considers that this does not adequately reflect the nature of some combinations such as donations of operations or some nationalizations.
76. Staff notes that where a combination occurs at market price, this is an indicator that the combination is an acquisition. Staff considers, however, that this factor provides less information than that provided by considering whether a combination includes consideration or is an exchange transaction.
77. Staff concludes that it is not necessary for an ED to consider whether a combination occurs at market price.

Distinguish between acquisitions NUCC and all other combinations

78. Respondents 8, 14 and 23 suggest that combinations could be distinguished between acquisitions NUCC and all other combinations.
79. Respondent 14 suggests this approach because
 - It is simpler than the approach suggested in the CP;
 - There are many combinations where no acquirer can be identified; and
 - The vast majority of combinations in the public sector do not involve the transfer of consideration.
80. Respondent 12 made similar comments but did not refer to consideration.
81. By proposing that it may be appropriate to apply the same accounting treatment to all combinations UCC, this Issues Paper partially addresses this proposal. Staff has yet to consider whether it would be appropriate to apply an identical accounting treatment to combinations UCC and amalgamations NUCC. This will be addressed in a later issues paper.
82. Staff notes that the proposal to distinguish between acquisitions NUCC and all other combinations does not provide any additional guidance as to when an acquisition occurs. Staff therefore concludes that this is not relevant to the development of an ED.

Combination has commercial substance

83. Respondent 26 proposed that whether a combination has commercial substance is a factor in determining whether a combination UCC is an acquisition or an amalgamation. The respondent did not define commercial substance.
84. Staff notes that no equivalent proposal was made in respect of combinations NUCC. Staff considers that in the absence of a definition of commercial substance, this factor will provide less information than that provided by considering whether a combination includes consideration or is an exchange transaction.
85. Staff concludes that it is not necessary for an ED to consider whether a combination has commercial substance.

The operation of Government, such as legislation, decrees and budget process

86. Respondents 5, 8, 11, 13, and 19 identify the operation of government as a factor that is relevant in determining whether one party to a combination has gained control. Respondent 11 suggests control would exist where the entity is accountable to Parliament, or the Executive or a particular Minister as evidenced by:
- The existence of a Ministerial or other government power enabling the government to direct the entity's governing body to achieve the government's policy objectives;
 - Ministerial approval is required for operating budgets;
 - The government has the ability to veto operating and capital budgets of the entity;
 - The government has broad discretion, under existing legislation, to appoint or remove a majority of the members of the governing body of the entity;
 - The entity is required to submit to Parliament reports on operations, including audited financial statements under legislative requirements applying generally to public sector entities or the entity's own enabling legislation; or
 - The mandate of the entity being established or limited by its enabling legislation.
87. Staff considers that this list of indicators is helpful in clarifying what respondents intended when referring to the operation of government. Staff notes that this list relates to the definition of control in ED 49, which is outside the scope of this project.
88. Staff does not consider this list to be helpful in determining whether one party has gained control when, for example, the combination is a combination of two municipalities that are not under the common control of central government.

Government has a residual financial interest in the net financial assets of the entity

89. Respondent 11 suggests that where a government has a residual financial interest in the net financial assets of the entity, this indicates that the government has control of that entity.
90. Staff considers that this factor may be relevant to the definition of control in ED 49, but is not conclusive. Staff does not consider this factor to be relevant in determining whether one party has gained control when, for example, the combination is a combination of two municipalities that are not under the common control of central government.

An entity is involved in directing public policy and/or engaging in non-market activity mainly financed by public resources

91. Respondent 13 comments that “the notion of control should, as we see it, be supplemented by the concepts of directing and/or executing public policies and engaging in non-market activity mainly financed by public resources.” Staff notes that this suggestion would require amendments to the definitions of an acquisition and an amalgamation.
92. Staff considers that this is contrary to the direction given by the IPSASB at the June 2014 meeting. At that meeting, the IPSASB requested staff to develop the classification of public sector combinations based on the proposals in the CP. Staff therefore concludes that this factor is not relevant to the development of an ED.

Matter(s) for Consideration

4. The IPSASB is asked to indicate whether it agrees with the staff conclusions that:
 - (a) Political control is unlikely to be relevant in identifying an amalgamation in a public sector combination;
 - (b) It is not necessary for an ED to consider whether a combination occurs at market price;
 - (c) The proposal to distinguish between acquisitions NUCC and all other combinations is not relevant to the development of an ED;
 - (d) It is not necessary for an ED to consider whether a combination has commercial substance;
 - (e) The operation of Government, such as legislation, decrees and budget process, is unlikely to be relevant in identifying an amalgamation in a public sector combination NUCC;
 - (f) Whether the government has a residual financial interest in the net financial assets of the entity is unlikely to be relevant in identifying an amalgamation in a public sector combination NUCC; and
 - (g) Whether an entity is involved in directing public policy and/or engaging in non-market activity mainly financed by public resources is not relevant in identifying an amalgamation in a public sector combination NUCC.

Alternative approach - no distinction between combinations NUCC

93. If the IPSASB does not support the proposals made by staff, it may conclude that it is not always possible to reliably determine whether one entity has gained control through a combination. This conclusion may be reached if the IPSASB concludes that the factors identified by staff, individually or in combination, do not provide sufficient guidance to determine a reliable boundary between acquisitions and amalgamations. This would be consistent with the conclusions reached by the IASB in developing IFRS 3.
94. BC35 in IFRS 3 notes that “the boards also observed that respondents and other constituents were unable to suggest an unambiguous and non-arbitrary boundary for distinguishing true mergers or mergers of equals from other business combinations and concluded that developing such an operational boundary would not be feasible.”
95. The IASB concluded that true mergers were rare in the private sector, and that the objectives of financial reporting in the private sector could be met by treating all combinations as acquisitions.

96. Many respondents to the CP commented that amalgamations are common in the public sector. The pragmatic approach adopted by the IASB may be more difficult to sustain in an IPSAS.

Joint Ventures

97. The CP excludes from its scope the formation of a joint venture. The reason given for this exclusion is that the presentation of a joint venture in the financial statements of the venturers is addressed in IPSAS 8. Staff notes that IPSAS 8 is being reviewed in the project on the Interests in Other Entities.
98. Accounting requirements for the formation of a joint venture in the financial statements of the joint venture itself are also excluded from the scope of the CP. The concept underlying the formation of a joint venture differs from other combinations, in that the formation arises from separate entities deciding to share control, i.e., they have joint control of the operations that form the joint venture. The concept of joint control may give rise to issues that affect how the joint venture itself should account for its formation. This exclusion is also consistent with the exclusion of joint ventures from the scope of IFRS 3.
99. Staff notes that the formation of a joint venture is the only combination of operations that is not covered by this project. Staff also notes that no respondent commented on this exclusion. As the concept underlying the formation of a joint venture differs from other combinations, staff considers that this exclusion of joint ventures from the scope of the project is appropriate. It may be appropriate to consider the accounting treatment of a joint venture in the financial statements of the joint venture itself in a later project. Staff notes there is no equivalent IFRS on this topic.

Matter(s) for Consideration

5. The IPSASB is asked **to confirm** its previous decision to exclude joint ventures from the scope of this project.

Next Steps

100. Once the IPSASB has agreed the approach to the classification of public sector combinations to be adopted in the ED, staff will develop further Issues Papers. These will cover:
- Accounting treatments. Staff notes that the pooling of interests method proposed by the CP will require further development to incorporate the combination of operations as well as entities. The combination of operations may give rise to differences that do not arise from the combination of entities. Staff notes that these differences could be treated as contributions from owners or distributions to owners for combinations UCC, but not amalgamations NUCC.
 - Measurement bases. These will be consistent with the Conceptual Framework.
 - Terminology. Staff notes that some respondents commented that the terminology used in the CP was confusing.
 - Presentation.

Matter(s) for Consideration

6. The IPSASB is asked **to note** the issues to be considered at future meetings.

APPENDIX A

CONSULTATION PAPER, *PUBLIC SECTOR COMBINATIONS* LIST OF RESPONDENTS

Response #	Respondent Name	Country	Function
001	Financial Management Standards Board (FMSB) of the Association of Government Accountants (AGA)	USA	Other
002	Cour des comptes	France	Audit Office
003	Conseil de normalisation des comptes publics (CNOCP)	France	Standard Setter/Standards Advisory Body
004	Charity Commission for England and Wales	UK	Other
005	Accounting and Auditing Standards Desk of the Abu Dhabi Accountability Authority (ADAA)	United Arab Emirates	Standard Setter/Standards Advisory Body
006	Australian Accounting Standards Board (AASB)	Australia	Standard Setter/Standards Advisory Body
007	Ernst & Young	International	Accountancy Firm
008	Heads of Treasuries Accounting and Reporting Advisory Committee (HoTARAC)	Australia	Preparer
009	The Japanese Institute of Certified Public Accountants (JICPA)	Japan	Member or Regional Body
010	Staff of the Accounting Standards Board	South Africa	Standard Setter/Standards Advisory Body
011	Australasian Council of Auditors-General (ACAG)	Australia	Audit Office
012	Chartered Institute of Public Finance and Accountancy (CIPFA)	UK	Member or Regional Body
013	Direction Générale des Finances Publiques (DGFIP)	France	Preparer
014	The Accounting Officer of the Commission, European Commission, DG Budget	Europe	Preparer
015	Office of the Comptroller General, Treasury Board of Canada	Canada	Preparer
016	Institut der Wirtschaftsprüfer (IDW)	Germany	Member or Regional Body

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Response #	Respondent Name	Country	Function
017	Institute of Certified Public Accountants of Kenya (ICPAK)	Kenya	Member or Regional Body
018	Institute of Chartered Accountants of Nigeria (ICAN)	Nigeria	Member or Regional Body
019	CPA Australia and the Institute of Chartered Accountants in Australia (ICAA)	Australia	Member or Regional Body
020	Staff of the Public Sector Accounting Board (PSAB)	Canada	Standard Setter/Standards Advisory Body
021	Zambia Institute of Chartered Accountants (ZICA)	Zambia	Member or Regional Body
022	The Public Sector Committee of the Institute of Chartered Accountants of Scotland (ICAS)	UK	Member or Regional Body
023	New Zealand Accounting Standards Board (NZASB)	New Zealand	Standard Setter/Standards Advisory Body
024	Denise Silva Ferreira Juvenal	Brazil	Other
025	Swiss Public Sector Financial Reporting Advisory Committee (SRS-CSPCP)	Switzerland	Standard Setter/Standards Advisory Body
026	The Committee on Accounting for Public Benefit Entities (CAPE) of the Financial Reporting Council (FRC)	UK	Standard Setter/Standards Advisory Body