

12 July 2016

Chief Executive
External Reporting Board
PO Box 11250
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New Zealand

Dear Warren

PBE Interests in Other Entities

The Treasury welcomes the opportunity to comment on exposure drafts relating to PBE interests in Other Entities:

- ED NZASB 2016-1 PBE IPSAS 34 *Separate Financial Statements*,
- ED NZASB 2016-2 PBE IPSAS 35 *Consolidated Financial Statements*,
- ED NZASB 2016-3 PBE IPSAS 36 *Investments in Associates and Joint Ventures*,
- ED NZASB 2016-4 PBE IPSAS 37 *Joint Arrangements* and
- ED NZASB 2016-5 PBE IPSAS 38 *Disclosure of Interests in Other Entities*.

The Treasury prepares the Financial Statements of the Government of New Zealand. These financial statements consolidate a significant number of entities, who for their own reporting purposes are a mix of Public Benefit Entities (PBEs) and for-profit entities (a "mixed group"). The Treasury therefore supports close alignment between PBE standards and for-profit standards where appropriate to avoid unnecessary differences and minimise the cost associated with mixed group issues. We are therefore pleased that these standards will substantially align the requirements in PBE standards with the requirements for for-profit entities.

We have provided our responses to the specified matters for comment in Annex One.

Yours sincerely



Nicola Haslam
Manager, Fiscal Reporting

Annex One: Invitation to comment – PBE Interests in Other Entities

Specific comments

ED NZASB 2016-1 PBE IPSAS 34 *Separate Financial Statements*

1. Do you agree that no substantive changes to IPSAS 34 are required to make it suitable for application by PBEs in New Zealand? If you disagree, please describe the additional changes that you consider to be appropriate.

The Treasury supports the proposal that no substantive changes are required to IPSAS 34 to make this standard suitable for application by PBEs in New Zealand.

In our submission to the IPSASB we suggested that they remove the option to use the equity method to account for investments in controlled entities, joint venture and associates of an entity that prepares separate financial statements. We consider the equity method to be a method of consolidation and therefore inappropriate to be used in non-consolidated financial statements. We are however relaxed about allowing the equity method to be used in the absence of cost information, as a deemed cost amount.

We note that the IPSASB considered this point in finalising IPSAS 34, but disagreed with the Treasury and maintained the equity option noting that this was also supported by the majority of respondents.

On the basis that there is merit in limiting differences between IPSAS 34 and PBE IPSAS 34, and the fact that it's an option rather than a requirement, we are comfortable that PBE IPSAS 34 is aligned with IPSAS 34.

ED NZASB 2016-2 PBE IPSAS 35 *Consolidated Financial Statements*

2. Do you consider that the IPSASB's reasons for retaining investment entity accounting in the financial statements of a non-investment controlling entity are relevant for both public sector and not-for-profit public benefit entities in New Zealand? If you do not agree, please explain why.

Yes, agree.

We are supportive of the investment entity exception and retaining this in the financial statements of a non-investment controlling entity.

We disagree with the IASB's reasons for limiting the investment entity exception and not allowing the same fair value accounting to flow up to the non-investment controlling entity. We note one of IASB's arguments was that this exception should be limited to the unique business model of the investment entity itself and the arguments for the exception is weakened when applied to the non-investment controlling entity. In our view, the non-investment controlling entity does not have a different view of the business model for this specific investment within the investment entity from the investment entity itself. We believe that fair value accounting of the investment in this limited circumstance is just as relevant for the non-investment controlling entity as the investment entity itself.

In New Zealand, the Government's sovereign wealth fund, the New Zealand Superannuation Fund (NZSF), meets the definition of an investment entity under IFRS 10 and as such fair values all its investments, whether it controls them or not. In our view, this treatment should be retained in the Financial Statements of the Government. There are many common users for both the financial statements of NZSF and the Government, such as parliament select committees and government ministers. Such users may be puzzled by different accounting for the same transaction and therefore question which treatment shows the "right answer".

We are comfortable with the IPSASB's reasons for retaining investment entity accounting in the financial statements of a non-investment controlling entity as set out in the Basis of Conclusion to IPSAS 3, paragraphs BC27 to BC 29.

3. Do you agree with how we have proposed to modify IPSAS 35 by including more guidance on predetermination (see paragraphs 21, 29.1, 35.1, AG8.1, AG53 and Example 29A)? If you do not agree, please explain why.

Yes, agree. The additional guidance is helpful in the New Zealand context as the role of pre-determination is pervasive and making judgments about this fact when determining whether one entity controls another is an area of significant debate.

4. Do you agree with the proposal to include integral application guidance on network and partner agreements in PBE IPSAS 35 (paragraphs AG31.1 to AG31.7)? If you do not agree, please explain why.

Yes, agree.

5. Do you agree with the other proposed modifications to IPSAS 35 in PBE IPSAS 35? If you disagree, please provide reasons and indicate the nature of any additional modifications that you consider to be appropriate.

Yes, agree. We are particularly pleased to see the inclusion in PBE IPSAS 35 of guidance on the application of consistent accounting policies in the consolidated financial statements and when the financial statements of a for-profit entity in a PBE group need to be restated in the preparation of consolidated financial statements.

ED NZASB 2016-3 PBE IPSAS 36 *Investments in Associates and Joint Ventures*

6. Do you agree that no substantive changes to IPSAS 36 are required to make it suitable for application by PBEs in New Zealand? If you disagree, please describe the additional changes that you consider to be appropriate.

Yes, agree.

ED NZASB 2016-4 PBE IPSAS 37 Joint Arrangements

7. Do you agree with the proposed modifications to IPSAS 37 in PBE IPSAS 37? If you disagree, please provide reasons and indicate the nature of any additional modifications that you consider to be appropriate.

Yes, agree.

ED NZASB 2016-5 PBE IPSAS 38 Disclosure of Interests in Other Entities

8. Do you agree that no substantive changes to IPSAS 38 are required to make it suitable for application by PBEs in New Zealand? If you disagree, please describe the additional changes that you consider to be appropriate.

We believe the definition of structured entities is confusing. The definition refers to entities where administrative or legislative factors, or voting or similar rights are normally the deciding factor in determining control, but where the structural design of the entity avoids those factors, for example by relying on binding arrangements.

Our confusion arises because:

- In the New Zealand public sector, binding arrangements are an administrative mechanism. Using binding arrangements in the structural design of an entity therefore does not avoid administrative factors being a deciding factor.
- We struggle with what is considered normal and what is abnormal. While a majority of public sector entities are established by legislation, it is fairly common for public sector entities not to have establishing legislation, for example the Treasury.

Having said that, the Treasury considers the administrative arrangements and legislation for accountability in the New Zealand government effectively resolve this problem. The schedules of entities in the Public Finance Act 1989 (PFA), Crown Entities Act 2004 and the State-Owned Enterprises Act 1986, while being legislative arrangements, apply generally accepted accounting practice (GAAP) to determine whether entities are controlled, no matter how they are structured. Given these schedules (and the "catch all" PFA section 27(3)(f) with reference to GAAP for entities not listed in these schedules) are used for determining the entities to be consolidated by the Government Reporting Entity, we believe there will be no structured entities for the New Zealand Government.

Based on that reasoning, and conscious of the merits of limiting the differences with IPSAS, the Treasury is not opposed to the inclusion of disclosure requirements on structured entities being retained in a PBE IPSAS 38. However, we believe the confusion should be highlighted to IPSASB and that this should be an area of focus for any post implementation review of the standard.

General

9. Do you agree with the Reduced Disclosure Regime concessions proposed in the EDs? If you disagree, please provide reasons and indicate any additional concessions that you consider would be appropriate.

Yes, agree.

10. Do you agree with the proposal that the final PBE Standards should have an effective date of 1 January 2019, with earlier application permitted?

We have no objection to this effective date, with earlier application being permitted.

11. Do you have any other comments on the EDs?

No.

