

Swiss Comment to

ED 60 Public Sector Combinations

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1. Introduction

The Swiss Public Sector Financial Reporting Advisory Committee (SRS-CSPCP) was established in 2008 by the Swiss Federal Ministry of Finance together with the cantonal Ministers of Finance. One of its aims is to provide the IPSAS Board with a consolidated statement for all three Swiss levels of government (municipalities, cantons and Confederation).

The SRS-CSPCP has discussed the *ED 60 Public Sector Combinations* and comments as follows.

2. General Remarks

The SRS-CSPCP is of the opinion that a standard for amalgamations and acquisitions is filling a gap in the current IPSAS literature. Already in its response to the *Consultation Paper* in September 2012 the SRS-CSPCP pointed out that acquisitions, in contrast to amalgamations, in the public sector are of very minor importance. The SRS-CSPCP continues to hold the view. However, it agrees that acquisitions can be included in a standard with a wider scope, as ED 60 is proposing.

The SRS-CSPCP has taken notice with satisfaction that the IPSASB has undertaken certain clarifications compared with the *Consultation Paper*. Some of these clarifications had been called for by the SRS-CSPCP. They are in particular the adoption of rules in connection with a popular referendum in the event of an amalgamation, for instance in the case of amalgamation of municipalities.

3. Specific Matter for Comment 1

Do you agree with the scope of the Exposure Draft? If not, what changes to the scope would you make?

The SRS-CSPCP is somewhat surprised that in the *ED*, as previously in the *Consultation Paper*, *Joint Ventures* and *Joint Operations* are explicitly excluded. It has, however, noted that in the Appendix to the *ED* it is proposed that IPSAS 37 will be changed in such a way that the new version of the standard will be applied for *Joint Ventures* and *Joint Operations*. The SRS-CSPCP therefore proposes that in the new standard on amalgamations and acquisitions a clear reference should be made to IPSAS 36/37. It would, however, be even better also to include *joint operations* in the new standard.

In Switzerland the concordats (i.e. arrangement between jurisdictions) and above all the joint operations (*Zweckverbände* in German or *associations de communes* in French) are of great significance. These latter are combinations of municipalities for the joint fulfilment of specific public services, which they are authorized or obliged to provide. In Switzerland joint operations are found above all in the area of schools, the supply of drinking water and the disposal of sewage and waste. Such an outsourcing of the tasks of municipalities to a joint operation could be understood as an "amalgamation" in order to provide the concerned public service. But according to the explanations of the IPSASB this would be a *joint operation* and therefore excluded from the standard. The SRS-CSPCP would be grateful to the IPSASB, if it could comment on this question and provide the necessary clarification.

In practice, based on the proposed standard, it would prove difficult to decide whether one is in a process of an amalgamation, of an acquisition or of a *joint operation/joint venture*. For this reason, the standard must better explain the difference between the various forms of combination. If the IPSAS Board wants to have two different standards on this topic, it must point out the difference between the new standard and IPSAS 36/37.

In the *Amendments to other IPSAS* - from page 97 (IPSAS 37.24A) – of ED 60 the treatment of the purchase of shares in a *joint operation* is laid down. Reference is made to the newly

introduced AG33A-AG33D. According to this, purchases of shares in a *joint operation* are to be recognized at fair market value (therefore IFRS 3). However ED 60 itself explicitly excludes the treatment of *Joint Arrangements (exclude from scope)*. Why then should the treatment of *Joint Operations* be included in the *Amendments*? In principle, nothing speaks against the extension of ED 60 principles to joint operations, if this is done transparently. I.e. it is irrelevant in which standard *the process of an amalgamation* is described, if it is made clear which standard needs to be applied in which circumstances.

In this consultation, there is no specific matter for comment on the extension of IPSAS 37. As the proposed standard is worded at the moment, only acquisitions for joint operations are governed, but not amalgamations. Therefore it suggests that there are no amalgamations in the case of *Joint Operations*. However this is clearly not the view of the SRS-CSPCP.

4. Specific Matter for Comment 2

Do you agree with the approach to classifying public sector combinations adopted in this Exposure Draft (see paragraphs 7–14 and AG10–AG50)? If not, how would you change the approach to classifying public sector combinations?

The SRS-CSPCP agrees with the statement that ‘control’ is a key element in distinguishing between amalgamations and acquisitions. However, the proposed standard makes no difference between the notion of control as understood in the private sector and the notion of control as it should be understood in the context of public authorities (e.g. municipalities). In this latter case and in the view of the SRS-CSPCP, the question is whether in an amalgamation of public authorities the citizen continues to have the suffrage and electoral rights in the newly created entity and therefore keeps on exercising a certain control. It is, however, obvious that a citizen living in a relatively small public authority must accept a relative loss of power in case this small public authority amalgamates with a larger one.

The addition of a second criterion (*rebuttable presumption*) is rather theoretical but nevertheless has the consequence that many combinations can be considered as amalgamations.

The decision tree (Figure 1 in the *Exposure Draft Summary*) is not very meaningful and concrete. Why not drawing up in the Appendix to the standard a more detailed decision tree with the categorisation criteria for amalgamation, acquisition, *Joint Ventures* and *Joint Operations*? Additionally, in this diagram a reference should be given in which standard the different “amalgamation forms” are considered. The illustration IG2 on page 122 of the ED can be used as a model.

5. Specific Matter for Comment 3

Do you agree that the modified pooling of interests method of accounting should be used in accounting for amalgamations? If not, what method of accounting should be used?

The SRS-CSPCP agrees that in amalgamation of public authorities the **Modified Pooling of Interest method** is applied. It would, however, be desirable that in the new standard an explanation is immediately given how the **Modified Pooling of Interest method** differs from the *Pooling of Interest method*. At present this difference can only be found in the Appendix (*Basis of Conclusion 43 – 44*).

It is often the case that amalgamated public authorities do not apply the same accounting principles in certain areas (e.g. pension fund commitments, useful working lives of assets, interest rates). Therefore, adjustments have to be made. These adjustments should be recognized in equity.

However, in the present ED it remains vague how exactly, for example, adjustments have to be made when amalgamating entities had previously considered different useful lives for the same kind of infrastructure assets or, more generally, had previously chosen a different

accounting option. For example, does the adjustment of the useful lives mean that all assets must be recalculated back to the date of acquisition in order to obtain the correct carrying amount in the opening balance sheet? If so, it is obviously no longer possible to claim that the **Modified Pooling of Interest method** is "seen as generally the least costly to apply". The IPSASB should add a corresponding clarification to ED 60.27 on how exactly amounts are to be derived.

6. Specific Matter for Comment 4

Do you agree to adjustments being made to the residual amount rather than other components of net assets/equity, for example the revaluation surplus? If not, where should adjustments be recognized?

Do you agree that the residual amount arising from an amalgamation should be recognized:

(a) In the case of an amalgamation under common control, as an ownership contribution or ownership distribution; and

(b) In the case of an amalgamation not under common control, directly in net assets/equity? If not, where should the residual amount be recognized?

The SRS-CSPCP wonders why *ownership contribution* and *ownership distribution* are mentioned. In connection with amalgamation of public authorities this is not relevant. The question also arises why *amalgamation under common control* and *amalgamation not under common control* should be treated differently. In both case the residual value should be recognized in equity.

7. Specific Matter for Comment 5

Do you agree that the acquisition method of accounting (as set out in IFRS 3, Business Combinations) should be used in accounting for acquisitions? If not, what method of accounting should be used?

The SRS-CSPCP agrees that the *acquisition method of accounting* under IFRS 3 should be applied in the event of acquisitions.

8. Final Remarks

As already noted when commenting on *ED 59 Employee Benefits* it is clear to the SRS-CSPCP that with the new standard the disclosure requirements will become much more demanding. If an entity wants to satisfy all the requirements, the Notes to the financial statements will be more extensive. This is not necessarily conducive to information. The SRS-CSPCP would therefore welcome it if the IPSASB could, following the materiality principle, declare only the most important disclosures to be necessary.

Lausanne, May 24, 2016