International Public Sector Accounting Standards (IPSAS) Workshop

Central Rift Branch

Presentation under IPSAS

Friday, 28 July 2017

Learning Outcome

- At the end of this session, delegates should:-
  - Understand and describe the components of financial statement;
  - Differentiate between changes in accounting policies, estimates and correction of errors;
  - Evaluate the existence of control; and
  - Explain the basis of consolidation under IPSAS accrual.

Content

IPSAS 1 – Presentation of Financial Statements

IPSAS 3 – Accounting Policies, Changes in in Accounting Estimates and Errors

IPSAS 6 – Consolidated and separate financial statements

Structure of IPSAS

- Recognition

- Measurement

- Disclosure

IPSAS 1

Effective date

- Issued in May 2000 and effective for annual periods beginning on or after January 1, 2008.

Scope

- All financial statements (FS) prepared in accordance with IPSAS

Objective

- To set out the manner in which general-purpose financial statements shall be prepared under the accrual basis of accounting, including guidance for their structure and the minimum requirements for content.

Components of Financial Statements

- A complete set of financial statements comprises:
  - Statement of financial position
  - Statement of financial performance
  - Statement of changes in net assets/equity
  - Cash flow statement
  - When the entity makes it approved budget publicly available, a comparison of budget and accrual amounts
  - Notes, comprising a summary of significant accounting policies and other explanatory notes

Overall Consideration

Compliance with IPSAS

- An entity whose financial statements comply with IPSAS shall make an **explicit and unreserved statement of such compliance** in the notes.

- Financial statements shall not be described as complying with IPSAS unless they comply with **all the requirements** of IPSAS.

Statement of Financial Position

- Include line items that present assets:
  - Property, plant and equipment;
  - Investment property;
  - Intangible assets;
  - Financial assets
  - Investments accounted for using the equity method;
  - Biological assets;
  - Inventories;
  - Trade and other receivables;
  - Current tax recoverable; and
  - Cash and cash equivalents; etc.

Statement of Financial Position (continued)

- Liabilities
  - Trade and other payables;
  - Provisions;
  - Financial liabilities
  - Liabilities for current tax,
  - Deferred tax liabilities
  - Liabilities included in disposal groups classified as held for sale
  - Finance lease obligations

- Equity
  - Net assets residual interest
  - Increased by surplus and
  - Reduced by deficit
  - Share capital (if any- some public sector entities will not have share capital)

True or false?

A financial asset is classified as current when it is held primarily for the purpose of being traded and it is expected to be realised between 12 and 24 months after the reporting period.

Current asset/liability

CURRENT ASSETS IF;

- Involved in normal operating cycle
- Held primarily for trading purposes
- Expected to be realised within 12 months
- Cash or a cash equivalent

CURRENT LIABILITIES IF;

- Involved in normal operating cycle
- Held primarily for trading purposes
- Due to be settled within 12 months
- No unconditional right to defer settlement for at least 12 months

Statement of Financial Performance

- All items of revenue and expenses recognized in the period shall be included in surplus or deficit unless an IPSAS requires otherwise

- As a minimum, the face of the statement of financial performance shall include line items that present the following amounts for the period:
  - Revenue;
  - Finance costs;
  - Share of the surplus or deficit of associates and joint ventures accounted for using the equity method;
  - Pre-tax gain or loss recognized on the disposal of assets or settlement of liabilities attributable to discontinuing operations; and
  - Surplus or deficit.

Classification of Expenses

- Analysis of expenses in the statement of financial performance may be given by
  i. nature; or
  ii. function.

- If presented by function, classification of expenses by nature should be provided as additional notes.

Classification of expenses (continued)

By nature:

Revenue		X
Employee benefits expense	X	
Depreciation and amortisation	X	
Other expenses	X	
Total expenses		(X)
Surplus		X

By function:

Revenue	X
Cost of sales	(X)
Distribution costs	(X)
Administrative expenses	(X)
Surplus	X

Other Comprehensive Income

- IPSAS 1 does not discuss the concept of OCI, however under the Implementation guidance (IG4), these items are presented directly in the statement of changes in net assets/equity.

- They include:-
  i. changes in revaluation surplus
  ii. actuarial gains and losses on defined benefit plans
  iii. gains and losses arising from translating the financial statements of a foreign operation
  iv. gains and losses on re-measuring available-for-sale financial
  v. the effective portion of gains and losses on hedging instruments in a cash flow hedge.

Statement of Changes in Net Assets

- An entity shall present a statement of changes in net assets/equity showing on the face of the statement:
  a. Surplus or deficit for the period;
  b. Each item of revenue and expense for the period that, as required by other Standards, is recognized directly in net assets/equity, and the total of these items;
  c. Total revenue and expense for the period (calculated as the sum of (a) and (b)), showing separately the total amounts attributable to owners of the controlling entity and to minority interest; and
  d. For each component of net assets/equity separately disclosed, the effects of changes in accounting policies and corrections of errors recognized in accordance with IPSAS 3.

Statement of Changes in Net Assets (continued)

- An entity shall also present, either on the face of the statement of changes in net assets/equity or in the notes:-
  a. The amounts of transactions with owners acting in their capacity as owners, showing separately distributions to owners;
  b. The balance of accumulated surpluses or deficits at the beginning of the period and at the reporting date, and the changes during the period; and
  c. To the extent that components of net assets/equity are separately disclosed, a reconciliation between the carrying amount of each component of net assets/equity at the beginning and the end of the period, separately disclosing each change.

Notes

- Present information in systematic order and cross reference to main statements. Normally presented in the following order:-
  - Statement of compliance with IPSAS
  - Bases of measurement and significant accounting policies applied
  - Supporting information required by IPSAS for items presented in the primary statements
  - Other disclosures e.g. contingent liabilities
  - Significant accounting policies
  - Management's judgements in applying accounting policies with significant effects on amounts recognised

IPSAS 3

Effective date

- IPSAS 3 was issued in May 2000 and became effective for annual periods beginning on or after January 1, 2008.

Scope

- Applicable to all financial statements (FS) in selection and applying accounting policies and accounting for changes in policies and prior period errors under IPSAS.

Objective

- To prescribe the criteria for **selecting** and **changing accounting policies,** together with the accounting treatment and disclosure of changes in accounting policies, **changes in accounting estimates** and the corrections of **errors.**

Accounting Policies

- Accounting policies
  - specific principles, bases, conventions, rules and practices applied by an entity in preparing and presenting financial statements.

Accounting Policies

- Selection
  - The accounting policies applied to an item (a transaction, other event or condition) are determined by
    - applying the IPSAS; and
    - considering any relevant Implementation Guidance issued by the IASB.

  - In the absence of an IPSAS that specifically applies to a transaction, other event or condition, management shall use its judgment in developing and applying an accounting policy that results in information that meets the qualitative characteristics

Accounting Policies

- Selection and application
  - The accounting policies applied to an item (a transaction, other event or condition) are determined by
    - applying the IPSAS; and
    - considering any relevant Implementation Guidance issued by the IASB.
  - In the absence of an IPSAS that specifically applies to a transaction, other event or condition, management shall use its judgment in developing and applying an accounting policy that results in information that meets the qualitative characteristics

Accounting policies

- **Consistency of Accounting Policies**
  - An organization shall select and apply its accounting policies consistently for similar transactions, other events and conditions, unless an IPSAS specifically requires or permits categorization of items for which different policies may be appropriate.
  - If a Standard requires or permits such categorization, an appropriate accounting policy shall be selected and applied consistently to each category.

Accounting policies

- **Changes in Accounting Policies**
  - An organization should only change its accounting policy only if the change:
    a. Is required by an IPSAS; or
    b. Results in the financial statements providing reliable and more relevant.
  - The effects of changes in accounting policies are presented as retrospective adjustments, unless the change is as a result of amendments in an IPSAS in which case the entity follows the transition guidelines in the IPSAS.

Accounting Policies

- *Disclosures*
  1. Title of the standard
  2. Transitional provisions, their nature and effect on the future
  3. The nature of the change in accounting policy
  4. Adjustments in the current period
  5. In case of impracticability, then the situation that led to that.

Changes in Accounting Estimates

- A change in accounting estimate is an **adjustment of the carrying amount of an asset or a liability,** or the amount of the periodic consumption of an asset, that results from the **assessment of the present status** of, and expected future benefits and obligations associated with, assets and liabilities.

- Changes in accounting estimates result from **new information or new developments** and, accordingly, are not corrections of errors.

- For example, estimates may be required, of:
  a) Bad debts arising from uncollected taxes;
  b) Inventory obsolescence;
  c) The fair value of financial assets or financial liabilities;
  d) Tax revenue due to government;
  e) The useful lives of, or expected pattern of consumption of future economic benefits or service potential embodied in depreciable assets, or the percentage completion of road construction; and
  f) Warranty obligations

Changes in Accounting Estimates

- The effect of a change in an accounting estimate, shall be recognized **prospectively** by including it in profit or loss in:
  a) the period of the change, if the change affects that period only; or
  b) the period of the change and future periods, if the change affects both.

- An entity shall **disclose** the nature and amount of a change in an accounting estimate that has an effect in the current period or is expected to have an effect on future periods, except for the disclosure of the effect on future periods when it is impracticable to estimate that effect.

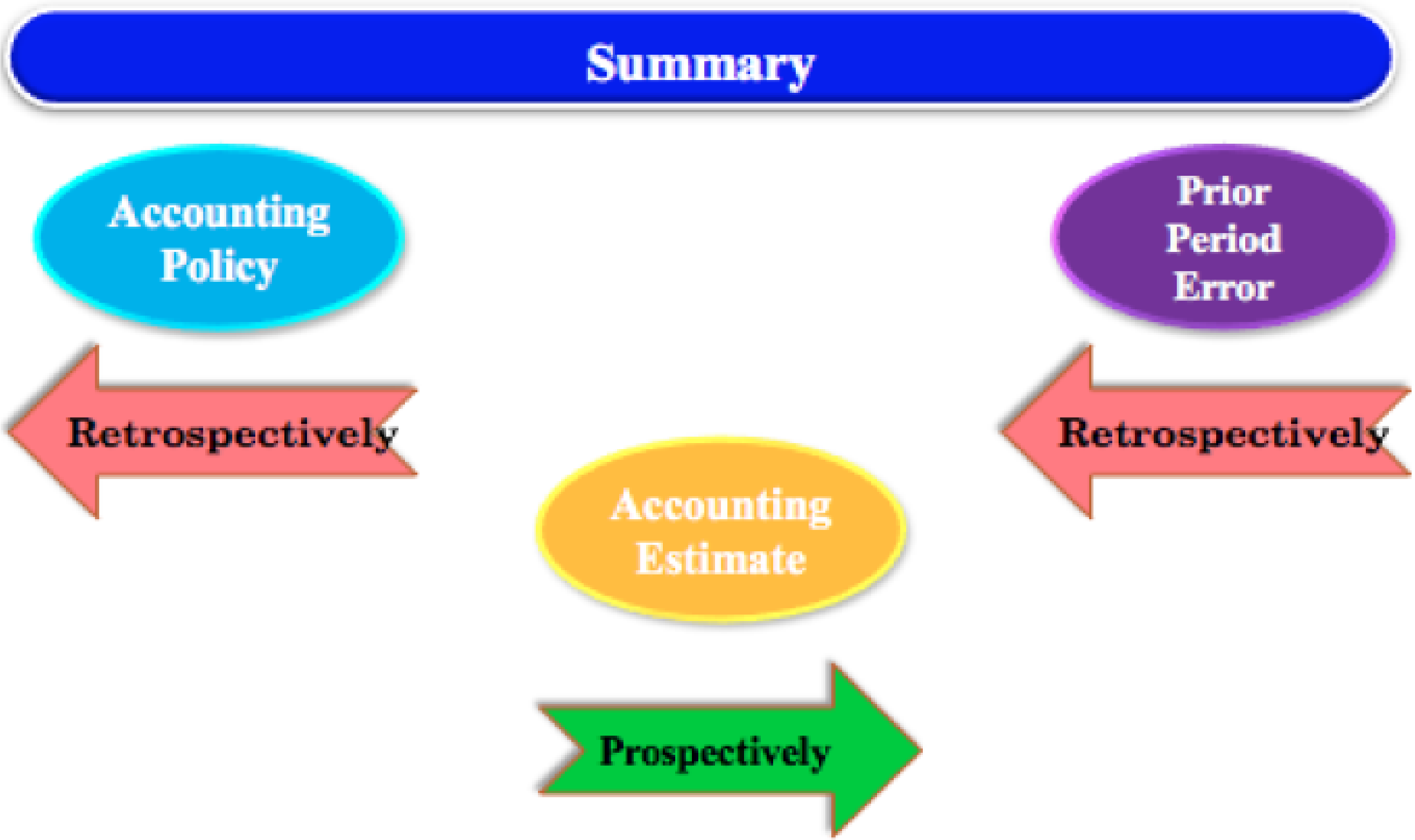
Prior Period Error

- Prior period errors are omissions from, and misstatements in, the entity's financial statements for one or more prior periods arising from a failure to use, or misuse of, reliable information that:-
  a) was available when financial statements for those periods were authorised for issue; and
  b) could reasonably be expected to have been obtained and taken into account in the preparation and presentation of those FS
  c) the effects of corrections of errors are presented as retrospective adjustments

Prior Period Error

- Disclosures
  a. The nature of the prior period error;
  b. For each prior period presented, to the extent practicable, the amount of the correction for each financial statement line item affected;

IPSAS 3 - Snapshot



IPSAS 6 – Consolidated and Separate Financial Statements

- Effective date
  - Annual periods beginning on or after January 1, 2008. *IPSASs 34-38 (Interests in Other Entities) are effective for annual periods beginning on or after 1 January 2017, replacing IPSASs 6-8. Earlier application permitted.*

- Objective
  - To prescribe requirements for preparing and presenting consolidated financial statements for an economic entity under the accrual basis of accounting. To prescribe how to account for investments in controlled entities, jointly controlled entities, and associates in separate financial statements.

IPSAS 6 (continued)

- A controlled entity is an entity controlled by another entity, known as the controlling entity.
- Control is the power to **govern the operating** and **financial policies.**
- Consolidated financial statements are financial statements of an economic entity (controlling entity and controlled entities combined) presented as those of a single entity.

IPSAS 6 (continued)

No need to consolidate if and only if

a) The controlling entity is itself a **wholly-owned controlled entity** or a partially-owned controlled entity of another entity and its other owners, have "approved"

b) The controlling entity's debt or equity instruments are **not traded in a publicly traded**

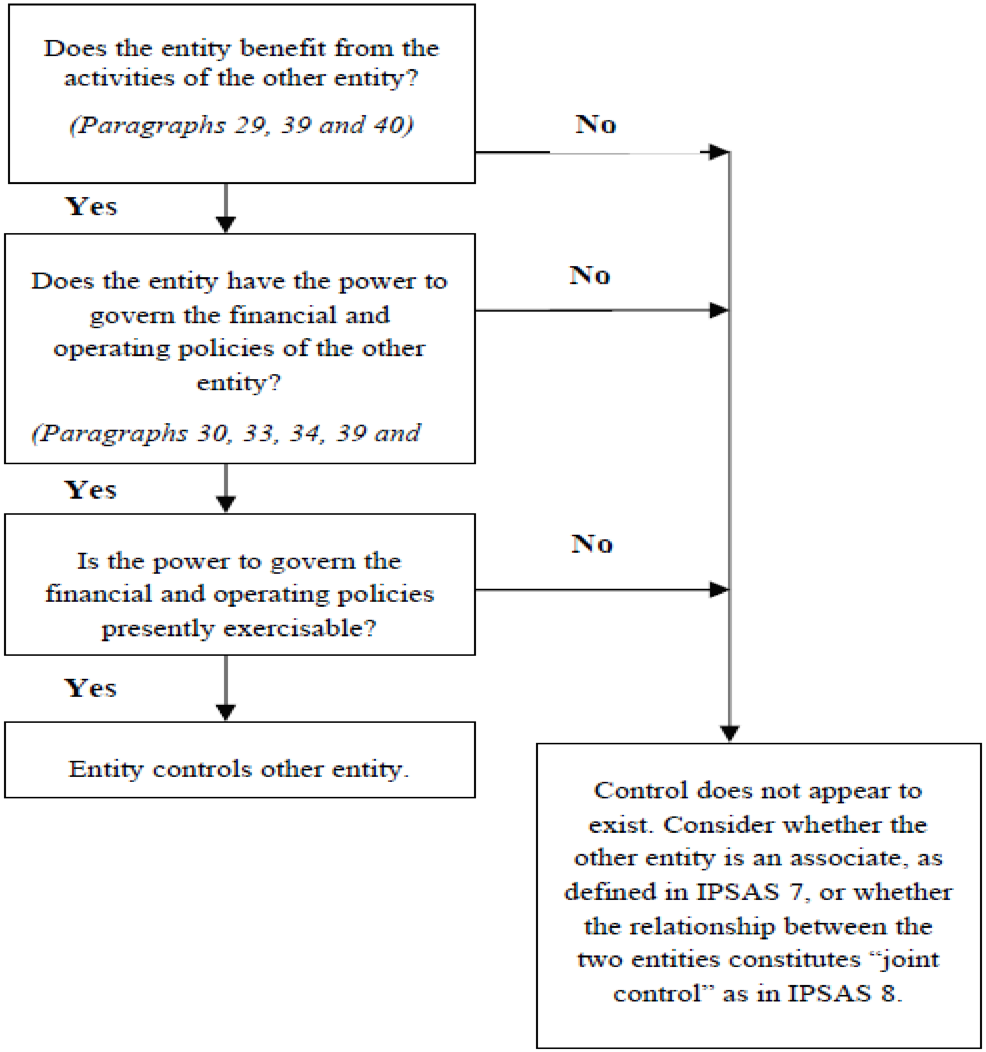
c) The controlling entity did not file, nor is it in the process of filing, its financial statements with a securities commission for **purposes of listing**; and

d) The ultimate or any intermediate controlling entity of the controlling entity produces consolidated IPSAS accrual financial statements and are publicly available

IPSAS 6 (continued)

- Consolidated financial statements shall include all controlled entities, except when there is evidence that:-
  - Control is intended to be temporary because the controlled entity is acquired and held exclusively with a view to its subsequent disposal within 12 months from acquisition; and
  - Management is actively seeking a buyer
- No exemption for controlled entity that operates under severe long-term funds transfer restrictions.
- A controlled entity is not excluded from consolidation because its activities are dissimilar to those of the other activities within the economic entity.

Establishing control



Does control exist?

- Entities A and B own 80% and 20% respectively of the ordinary shares that carry voting rights at a general meeting of shareholders of Entity C. Entity A sells one-half of its interest to Entity D and buys call options from Entity D that are exercisable at any time at a premium to the market price when issued, and if exercised would give Entity A its original 80% ownership interest and voting rights.

Does control exist?

- *Though the options are out of the money, they are currently exercisable and give Entity A the power to continue to set the operating and financial policies of Entity C, because Entity A could exercise its options now. The existence of the potential voting rights, as well as the other factors described in paragraphs 39 and 40 of IPSAS 6, are considered and it is determined that Entity A controls Entity C.*

Does control exist?

- Entities A and B own 55 % and 45% respectively of the ordinary shares that carry voting rights at a general meeting of shareholders of Entity C. Entity B also holds debt instruments that are convertible into ordinary shares of Entity C. The debt can be converted at a substantial price, in comparison with Entity B's net assets, at any time and if converted would require Entity B to borrow additional funds to make the payment. If the debt were to be converted, Entity B would hold 70% of the voting rights and Entity A's interest would reduce to 30%.

Does control exist?

- *Although the debt instruments are convertible at a substantial price, they are currently convertible and the conversion feature gives Entity B the power to set the operating and financial policies of Entity C. The existence of the potential voting rights, as well as the other factors described in paragraphs 39 and 40 of IPSAS 6, are considered and it is determined that Entity B, not Entity A, controls Entity C. The financial ability of Entity B to pay the conversion price does not influence the assessment.*

IPSAS 6 (continued)

- Consolidation Procedures
  - Balances, transactions, revenue, and expenses between entities within the economic entity are eliminated in full*
  - Use uniform accounting policies for like transactions and other events in similar circumstances.
  - Reporting dates of controlled entities cannot be more than three months different from reporting date of the controlling entity.

IPSAS 6 (continued)

- Consolidation Procedures
  - Minority interest is reported in net assets/equity in the consolidated statement of financial position, separately from the controlling entity's net assets/equity, and is not deducted in measuring the economic entity's revenue or expense.
  - Surplus or deficit of the economic entity is **allocated between minority and majority interest on the face** of the statement of financial performance.
  - In the controlling entity's separate financial statements: Account for all of its investments in controlling entities, associates, and joint ventures either using the equity method, at cost or as financial instruments.

IPSAS 6 - Disclosure

- Include:

a. A list of significant controlled entities;

b. The fact that a controlled entity is not consolidated (if any)

c. Summarized financial information of controlled entities, either individually or in groups, that are not consolidated, including the amounts of total assets, total liabilities, revenues and surplus or deficit;

d. The name of any controlled entity in which the controlling entity holds an ownership interest and/or voting rights of 50% or less, together with an explanation of how control exists;

IPSAS 6 - Disclosure

- Include (continued)

e. The reasons why the ownership interest of more than 50% of the voting or potential voting power of an investee does not constitute control;

f. The reporting date of the financial statements of a controlled entity (if different); and

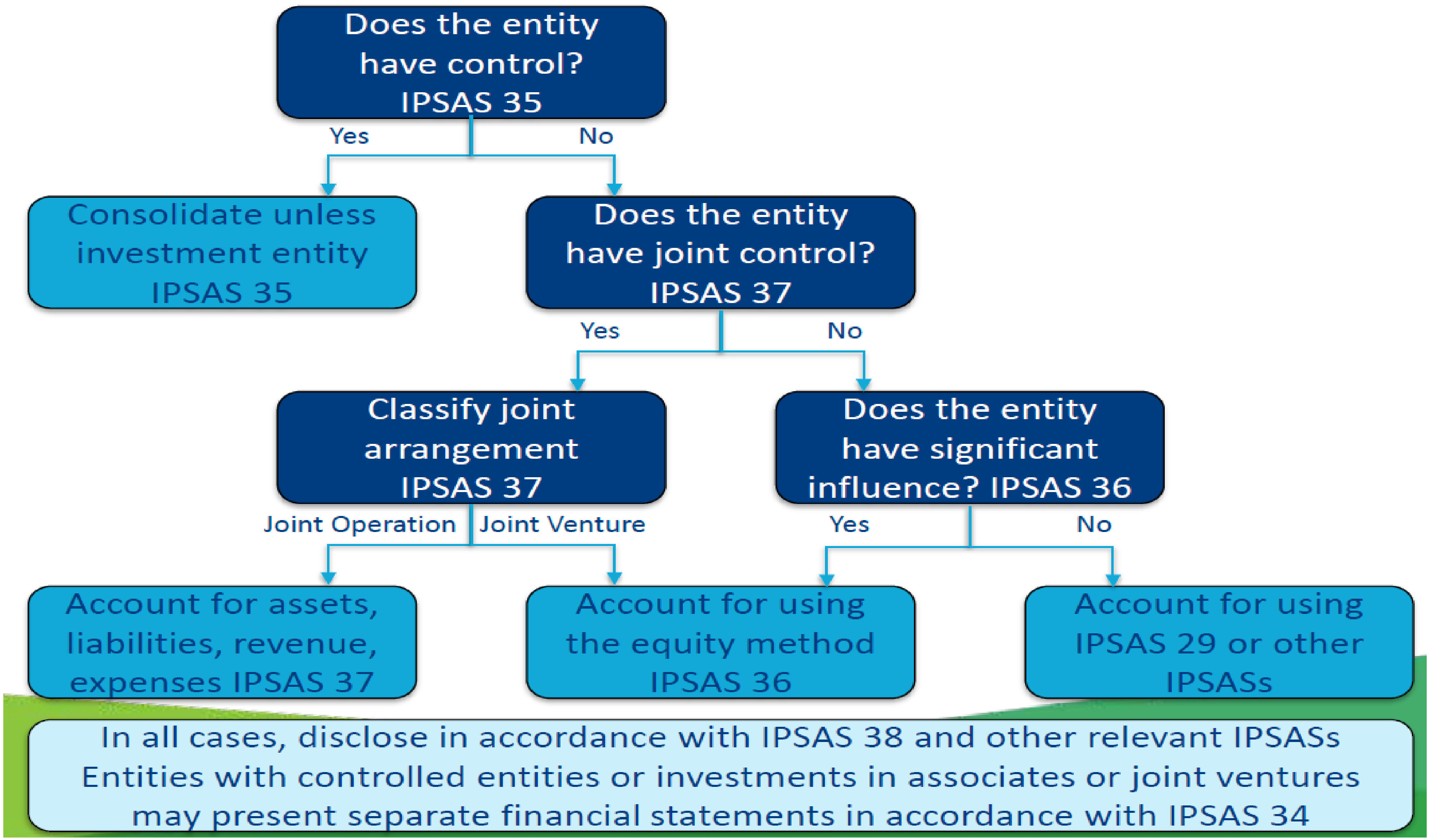
g. The nature and extent of any significant restrictions on the ability of controlled entities to transfer funds to the controlling entity.

IPSAS 34-38 Accounting for Interest in Other Entities

- Accounting for Interest in Other Entities
  - IPSAS 34 – Separate Financial Statements
  - IPSAS 35 - Consolidated Financial Statements
  - IPSAS 36 - Investments in Associates and Joint Ventures
  - IPSAS 37 - Joint Arrangements
  - IPSAS 38 - Disclosure of Interest in Other Entities

  - Replaces the current requirements in IPSAS 6, *Consolidated and Separate Financial Statements*; IPSAS 7, *Investments in Associates*; and IPSAS 8, *Interests in Joint Ventures*.

  - Annual financial statements covering periods beginning on or after January 1, 2017. Earlier application is encouraged.


Does the entity have control? IPSAS 35
Yes
No
Consolidate unless investment entity IPSAS 35
Does the entity have joint control? IPSAS 37
Yes
No
Classify joint arrangement IPSAS 37
Does the entity have significant influence? IPSAS 36
Joint Operation
Joint Venture
Yes
No
Account for assets, liabilities, revenue, expenses IPSAS 37
Account for using the equity method IPSAS 36
Account for using IPSAS 29 or other IPSASs
In all cases, disclose in accordance with IPSAS 38 and other relevant IPSASs
Entities with controlled entities or investments in associates or joint ventures may present separate financial statements in accordance with IPSAS 34

Interactive Session

- http://www.treasury.go.ke/financial-reporting-templates/consolidated-financial-statements.html
- http://www.treasury.go.ke/financial-reporting-templates-2.html


THANK
YOU!