

30 June 2016

Mr. John Stanford  
International Public Sector Accounting  
Standards Board  
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submitted electronically through the IPSASB website

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## **Re.: Proposed International Public Sector Accounting Standard (IPSAS), Public Sector Combinations**

Dear Mr. Stanford,

The IDW would like to thank you for the opportunity to provide the International Public Sector Accounting Standards Board (IPSASB) with our comments on the Exposure Draft “Public Sector Combinations” (hereinafter referred to as “the ED”).

This letter includes general comments. We respond to the Specific Matters for Comment (SMCs) in the appendix.

### **General comments**

As the IDW previously commented in its response to the Consultation Paper: Public Sector Combinations issued in 2012, we support this initiative and believe that entity combinations constitute an important public-sector specific hitherto not specifically addressed in the Suite of IPSASs. We agree that the current reference to IFRS is not helpful.

We agree with the Board that public sector combinations often differ from the profit-oriented mergers and acquisitions generally observed involving companies in the private sector, and thus support the IPSASB’s efforts to

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develop this ED tailored to the public sector environment to deal with the differentiation between amalgamations and acquisitions.

Although we generally agree with the proposals we have a few concerns as to terminology and the wording of certain definitions. In addition, for reasons of simplicity in application, and in order to limit subjectivity, we suggest the final Standard require depreciation of goodwill arising in the event of an acquisition. We refer to the appendix for further details of these and other concerns.

If you have any questions relating to our comments in this letter, we should be pleased to discuss matters further with you.

Yours truly,

Klaus-Peter Feld  
Executive Director

Gillian G. Waldbauer  
Head of International Affairs

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## Appendix

### **Specific Matters for Comment**

#### **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?*

We agree with the proposed scope of the ED, and the explicit exclusions listed in paragraph 3.

In our opinion it is particularly important for the IPSASB to clarify, but also to explain in the BCs the reasons for the scope in this project. For example whilst it might be relatively clear that transactions such as the nationalization of a particular company or industry should fall within a standard on public sector combinations, we believe that clarification of the required accounting treatment may be particularly necessary when public sector entities are involved in what might be initially intended as relatively temporary measures e.g., the bailout of a strategically important private sector entity.

We also agree with the recognition that not only entities may combine and thus support the introduction of the term “operation” to deal with this phenomenon, as this may occur relatively often in practice.

#### **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?*

Yes. However, we have the following comments:

#### **Amalgamations**

On reading the ED there appears to be an implicit presumption that a combination of operations which are subject to common control will always constitute an amalgamation. We suggest this be reflected in the definition (see below under the subheading “Definitions”).

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### Acquisitions

We agree that a gain of control is an indicative factor in the determination of whether a combination should be classified as an acquisition, and that a gain of control alone may not necessarily equate, in substance, with an acquisition.

In addition, we support the concept of a rebuttable presumption supported by consideration of specific further factors as preferable to the so-called individual weighting approach, since the latter introduces a higher degree of subjectivity.

In our opinion, the factors listed to be taken into account in deciding whether the economic substance of the transaction is such that it would be classified as an amalgamation, notwithstanding the fact that one party gains control over another or over an operation, need to reflect the economic substance of the “end product” (for example whether control has been gained in substance or only in form – i.e., how is the control gained actually exercised in practice) and not just factors such as consideration and decision making, which are both formal procedural factors.

### Definitions

We have commented on the definition of amalgamations above. We also find the proposed inclusion of the rebuttable presumption placed within definitions of amalgamation and acquisition makes for circular definitions, which are awkward. We suggest the two definitions be revised along the lines of:

“An amalgamation is .....

- (a) ...
- (b) All parties to the combination are under common control of another party, or
- (c) A public sector combination in which
  - a. one party to the combination gains control of one or more operations;  
and
  - b. no further factors exist that are persuasive that the economic substance of the transaction is that of an acquisition.”

“An acquisition is a public sector combination in which

- (a) one party to the combination gains control of one or more operations; and
- (b) one or more further factors exist that are persuasive that the economic substance of the transaction is that of an acquisition.”

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**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?*

Subject to our comments concerning terminology, we agree that the modified pooling of interests method of accounting is likely to be a more appropriate method than the fresh-start approach.

We also agree that the modification to the pooling of interests method (i.e., from the date of amalgamation going forward) better reflects the substance of the amalgamation, provided information users need about the history is disclosed.

We still hold our previously expressed view that the term “modified pooling of interests method” could be misunderstood, particularly by those familiar with the pooling of interests method. In responding to the CP we had proposed a different term be introduced, but note that this issue was not taken up by the IPSASB and is not discussed in the draft BC.

**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?*

In our view, the ED proposals represent the most appropriate treatment for any adjustments arising on amalgamation.

*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?*

We agree with the proposed treatment outlined above.

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**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?*

We agree that an acquisition method of accounting analogue to IFRS 3 will generally be appropriate for acquisitions within the public sector.

We also refer to our response to the consultation in which we suggested the Board consider prescribing the amortization of goodwill resulting from an acquisition in the public sector over time, and disallow the impairment-only approach. The cost model is likely to be less costly to apply and involves far less subjectivity than the revaluation model, under which impairment testing (IPSAS 26) would apply.

We appreciate that ED 60 governs the subsequent treatment of only a few selected items, referring to existing IPSASs in regard to other assets. Were the IPSASB to decide to follow our suggestion, we suggest the Board consider whether this aspect could also be addressed in the section headed “subsequent measurement and accounting” immediately preceding paragraph 46 of ED 60, or, alternatively, be dealt with by limiting the choice of methods currently permitted in paragraph 71 of IPSAS 31 specifically for goodwill arising from acquisitions.