Audit New Zealand
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Financial reporting update for central government update and Crown entities, April 2014

1. Changes for June 2014

Public benefit entities

- No new standards

For-profit entities

New standards for groups, associates and joint ventures (now called Joint Arrangements)

- These standards only apply where the parent or the investor is a for-profit entity
    - Public benefit entities (PBEs) continue to use the old version of the equivalent standards.
    - The old and new Standards are shown in the table below – there isn't an exact one-for-one match – together with a brief outline of the new Standards.
- Definitions of 'subsidiary' and 'joint arrangements' have changed slightly
    - May mean some special purpose entities are now considered to be 'controlled' and thus need to be consolidated (that weren't previously).
- Accounting for some 'joint arrangements' may change as may now be differently classified.
    - If a joint venture, then <u>must</u> equity account; previously could do proportionate consolidation
    - If a joint operation, then proportionate consolidation may previously have been equity accounted.
- Will be an issue for PBEs with for-profit group structures (e.g. Crown and State Owned Enterprises) as they will be applying one set of Standards for the 'for-profit' group and another at the whole-of-government level.

New standard for Fair Value Measurement [NZ IFRS 13]

- Single framework for measuring fair value.
- Applies wherever a Standard requires an entity to measure assets or liabilities at fair value.
- Not applicable for PBEs, but could be used by them as guidance.

The new group, associate and joint arrangements standards

PBE/Old NZ IFRS	**For-Profit NZ IFRS**	
NZ IAS 27 (PBE) *Consolidated and separate financial statements*	NZ IAS 27: *Separate financial statements*	This has the "separate financial statements" part of the old NZ IAS 27: • how to account for interests in subsidiaries, associates and joint ventures in the separate financial statements (cost, or as a financial instrument); • disclosures when taking the exemption not to consolidate.
	NZ IFRS 10: *Consolidated financial statements*	• criteria to determine whether or not a group exists; • consolidation procedures; • transition provisions.
NZ IAS 28 (PBE) *Investment in Associates*	NZ IAS 28 *Investments in Associates and Joint Ventures*	• criteria to determine whether an investment is an associate; • equity accounting procedures (for both associates and JVs).
NZ IAS 31 (PBE) *Interests in Joint Ventures*	NZ IFRS 1: *Joint Arrangements*	• criteria to determine whether or not an entity has a joint arrangement, and what type it is: joint operation or joint venture [*may differ from NZ IAS 31*]; • how to account for each type: line-by-line consolidation or equity-accounting (*if equity, then go to NZ IAS 28*; • transitional provisions.
Each of the old standards had: • criteria for determining if it applies; • the accounting requirements,and Disclosures	NZ IFRS 12: *Disclosure of Interests in Other Entities*	Disclosure requirements for interests in: • subsidiaries; • associates and joint arrangements; • unconsolidated structured entities.

2. The new framework

For-profit entities: continuing with standards based on International Financial Reporting Standards (IFRS) as issued for commercial entities

- private sector entities
- for-profit entities in the public sector (for example SOEs, CRIs)

Public benefit entities: using standards based on International Public Sector Accounting Standards (IPSAS) issued by the International Public Sector Accounting Standards Board.

- **Public sector** (for example departments, most Crown entities, local authorities);
- Not-for-profit entities.

3. Transition timeframe

First reporting date under the new standards: 30 June 2015

- the comparative information will need to be restated so that it complies with the new standards;
- that means entities will need to prepare an IPSAS-compliant balance sheet as at 1 July 2013;
- the transition requirements, including disclosures, are in PBE FRS-46 [see XRB website]; and
- the disclosure requirements are much less onerous than when we transitioned to IFRS.

For entities with balance dates other than June, the timeframe will be:

Balance date	Opening balance sheet	Apply new Standards	First reporting under new framework
December	1 January 2014	1 January 2015	31 December 2015
March	1 April 2014	1 April 2015	31 March 2016

Entities are not permitted to early adopt the new framework.

4. Tiers

The new reporting regime introduces a Tier-structure which determines the accounting standards and disclosure requirements that entities apply. There are four Tiers, although the first two are the ones that will apply to government departments and most Crown entities.

The criteria for each Tier, and the standards and disclosures are as follows: all entities start at Tier 1; they can move to a lower Tier if they meet the criteria.

PBE Tier structure

Tier	Criteria	Accounting Standards
1	Expenditure more than $30m *or* public accountability	PBE Accounting Standards (PAS)
2	Expenditure less than $30m and not publicly accountable	PAS with Reduced Disclosure Requirements (RDR)
3	Expenditure less than $2m and not publicly accountable	Simple Format Reporting (SFR) – accrual
4	Entities allowed by law to use cash accounting and operating payments less than $125k	SFR - cash

For-profit Tier structure

Tier	Criteria	Accounting Standards
1	Expenditure more than $30m *or* public accountability (as defined)	Full NZ IFRS
2	Expenditure less than $30m and not publicly accountable	NZ IFRS with Reduced Disclosure Requirements (RDR)
3	Not publicly accountable and either all of its owners are members of the entity's governing body or not large. If an entity's parent or ultimate controlling party has the coercive power to tax, rate or levy, it must satisfy the not large criterion	NZ IFRS Differential Reporting This tier will be removed for periods beginning on or after 1 April 2015.
4	Applied Old GAAP at 30 June 2011, not publicly accountable, not required to file financial statements under section 19 of the FRA and not large	Old GAAP This tier will be removed for periods beginning on or after 1 April 2015.

About the PBE Tier structure

Difference between TIER 1 and TIER 2

The only difference between TIER 1 and TIER 2 is the level of disclosure. The accounting Standards are the same and there are no exemptions from accounting treatment. For example:

- Under Differential Reporting an entity could elect not to prepare a cash-flow statement; and
- under RDR a TIER 2 entity will have to prepare a cash-flow statement, but there are exemptions from some of the disclosures.

Tier 3 is different

Has its own Accounting Standard [PBE SFR-A: see XRB website]

Only 50 pages instead of the suite of Standards for Tier 1 and Tier 2. As a result there will be a number of situations where the standard does not provide sufficient or any guidance. Where the standard does not give guidance the process to follow is in this order:

- principles and requirements of SFR-A dealing with similar or related events;
- definitions and concepts in the PBE framework to the extent they do not conflict with SFR-A;
- may also consider (but not required to apply) relevant requirements of Tier 2 standards; and
- can elect to opt-up for transactions already covered by SFR-A

The Standard also sets out how information is to be presented.

Criteria for Tier 1 and Tier 2

Expenditure > $30m:

Take into account all expenses/losses included in surplus/deficit.

- determined by the expenses in the financial statements, *not* by what the forecast expenditure was; and
- don't include items in Other Comprehensive Income.

Department and Crown expenditure considered separately.

- for example: if departmental expenditure is $10m and Crown expenses are $50M then department could report as Tier 2, but the Crown information will require all the Tier 1 disclosures.

Where there is a group

- For the group, the Tier is determined by the expenditure in the consolidated financial statements
- Parent: use same Tier as for the group

- Assess subsidiaries individually; if a subsidiary's expenditure is less than $2m and the subsidiary is not 'publicly accountable' then it could use TIER 3 reporting

Publicly accountable if:

- shares or debt are traded; and
- a reporting entity under the Financial Markets Conduct Act.

Departments will not be 'publicly accountable'. There may be a few Crown entities that need to check.

Moving between Tiers

- If become 'publicly accountable' then have to move to Tier 1 immediately.
- If become eligible for a lower Tier: then can move immediately.
- If have to move up because expenditure increases, can delay the change.

From Tier 2 to Tier 1: can defer change to the year <u>after</u> become large, for example:

Expenditure in 2015: $28m	Can apply TIER 2 reduced disclosure regime
Expenditure in 2016: $32m	Can still apply TIER 2 RDR, but could move to TIER 1.
Expenditure in 2017: $33m	Must move to TIER 1

From Tier 3 to Tier 2: can defer movement for <u>two years</u>, for example:

Expenditure in 2015: $1.5m	Can apply TIER 3 reduced disclosure regime
Expenditure in 2016: $2.3m	Can still apply TIER 3, but could move to TIER 2 (RDR)
Expenditure in 2017: $2.3m	Can still apply TIER 3, but could move to TIER 2 (RDR)
Expenditure in 2018: $2.3m	Must move to TIER 2

5. Reduced Disclosure Requirements under IPSAS

Overview

- Provides an opportunity for eligible entities to reduce their disclosures
- More entities will be eligible compared to differential reporting
- Disclosures identified in the Standards with an asterisk (*) are not required
- Paragraphs that start with "RDR" can be applied
    - o Some disclosure still required, but simplified
- Entities can "cherry pick" which concessions that they apply

- If a concession is no longer applied, comparative information is required (unless that particular disclosure does not require comparative information)

Opportunities to reduce disclosures

Opportunities to reduce disclosures that will apply in most circumstances include:

- financial instruments;
- capital management;
- reconciliation of surplus/deficit to net operating cash flows;
- standards issued and not yet effective
- prior year opening to closing reconciliations (for example, PPE).

Opportunities to reduce disclosures that will apply in certain circumstances include:

- asset and goodwill impairments;
- associate investments;
- income tax;
- agricultural activities; and
- when business combinations occur.

PBE RDR compared to differential reporting

For an entity currently using differential reporting exemptions, the main effects of moving to RDR include:

- no recognition and measurement concessions under RDR;
- cannot use income tax depreciation rates;
- intangible development costs must be capitalised;
- all biological assets must be measured at fair value;
- fewer presentation concessions under RDR;
- must prepare a statement of cash flows; and
- must prepare a statement of changes in equity.

6. Transition

The transitional provisions for Tier 1 and Tier 2 public sector entities are set out in PBE FRS 46 *First-Time Adoption of PBE Standards by Entities Previously Applying NZ IFRSs*

Overview of PBE FRS 46

PBE FRS-46 applies to:

- the first annual financial statements prepared using PBE Standards;
- each interim financial report during the financial year of first-time application of PBE Standards;
- prospective financial statements of the year of first-time application of PBE Standards; and

In transitioning, use same policies as applied under NZ IFRS (PBE) unless:

- PBE Standards **require** a change;
- there is a voluntary change in accounting policy; or
- a prior period error is identified;

Specific transitional provisions apply in some circumstances

Opening statement of financial position

Prepare an opening statement of financial position at transition date (for example, 1 July 2013 for June year-end entities):

- apply the PBE standards effective at the reporting date of first PBE financials; that is, the Standards that are effective at the <u>end</u> of the first reporting period. That balance sheet does not need to be disclosed;
- accounting policies used must be consistent throughout all periods presented in the first financial statements under PBE Standards;
- adjustments recognised in opening equity; that is, at transition date.

For items recognised for first-time with no specific transitional provision, option to measure using 1 of 3 approaches:

- retrospective approach following PBE IPSAS 3;
- fair value at date of transition;
- fair value measure as deemed cost at date of transition; which must be a value determined in accordance with PBE Standards, or NZ IFRS determined at or before the date of transition to PBE Standards.

Stable platform?

- Expect standards will be stable during transition, but could well be changes soon after transition [for example, the new IFRS Standards for Group, Associates and Joint Ventures].

Comparatives

Amounts restated for adjustments arising on transition.

Comparative information is amended for classification or presentation changes arising on transition.

Specific transitional provisions

For grantor service concession arrangements (SCAs) not previously accounted for under IPSAS 32, either:

- Apply PBE IPSAS 32 retrospectively; or
- Recognise SCA assets (based on a fair value measurement) and related liabilities at their deemed cost at the date of transition

Specific transitional provisions: when differential reporting previously applied

If concessions of NZ IAS 16, NZ IAS 21, NZ IAS 38 or NZ IAS 41 were applied, either:

- apply requirements of equivalent PBE IPSAS standard retrospectively; or
- apply the transitional provisions of FRS-46.

Transitional provisions of FRS-46:

- Change in depreciation or amortisation rates treated as a change in estimate at the date of transition
- Development costs capitalised from date of transition prospectively
- Foreign currency transactions accounted under PBE IPSAS 4 prospectively from date of transition
- The cost of agricultural produce harvested prior to date of transition measured at previously determined amount for purposes of PBE IPSAS 12 *Inventories*

Cash flow statement comparatives required.

Deferred tax measured retrospectively.

Disclosure

Para 40 – Disclose a statement that first financial statements prepared under PBE Standards

Para 42 – Disclose the nature and amount of the adjustment for each financial statement line item materially affected at date of transition. Separate:

- correction of errors;
- voluntary changes in accounting policies; and
- changes arising from transition to PBE Standards

Para 18 - For changes in presentation or classification, disclose:

- nature of reclassification;
- amount of each item reclassified; and

- reason for the reclassification

7. Transition tools

Transition Guidance

- Outline of the differences between the new IPSAS Standards and NZ IFRS

Model Financial Statements

- will have full Tier 1 disclosures; and
- will also show which disclosures are optional under Tier 2.