

2016

Financial Reporting Consolidation

PEMPAL Treasury Community of Practice
thematic group on Public Sector Accounting
and Reporting



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1 Goals and target audience for the Guidance Note

1.1 Goals of the Guidelines

The goal of this Guideline is to support governments and public sector officials in the process of preparing and presenting consolidated financial information on the public sector and entities within the public sector.

Although many countries have achieved some degree of consolidation, few have been able to present consolidated whole of government information for all controlled entities at the national level. The Guidance note considers the constraints, both conceptual and practical, to such consolidated information. Consideration is given to the benefits of consolidated information in terms of transparency and accountability as well as the costs and difficulties of consolidation. Methodologies are suggested for a phased approach to consolidation, the presentation and publication of consolidated information. There is also guidance on the use of such consolidated information by civil society organisations.

1.2 Target Audience

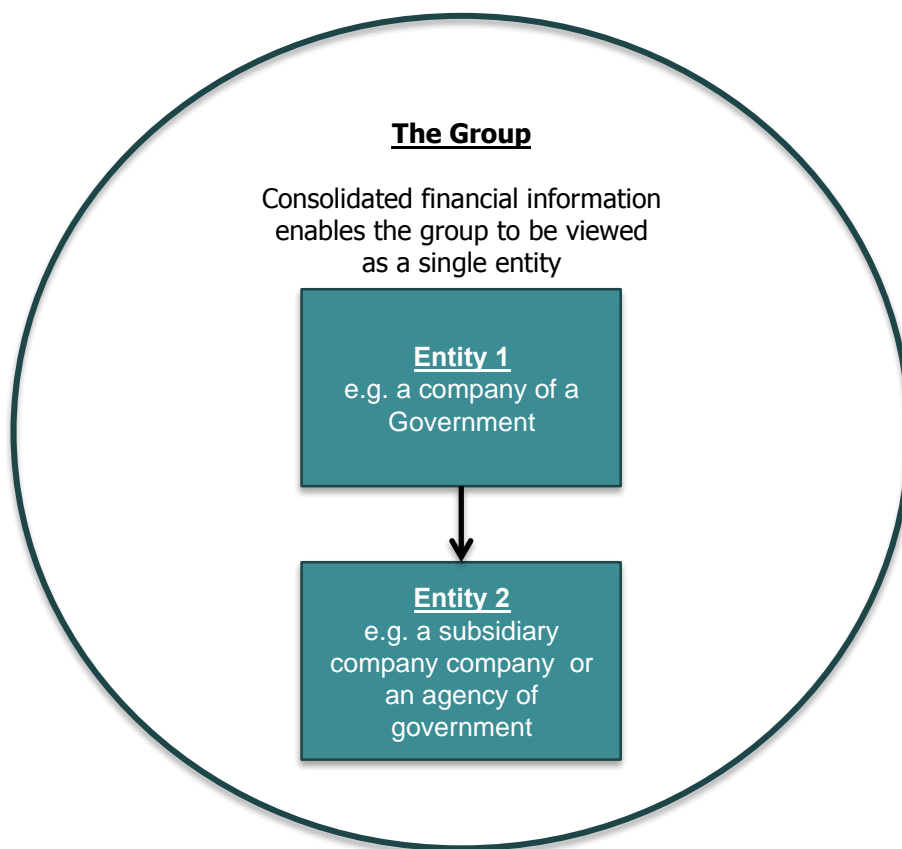
The primary target audience for this Guidance are the public officials who must undertake the consolidation, prepare and publish consolidated information. The Guidance may also be useful to those who advise such public sector officials, their political leaders and civil society organisations that use the information.

2 Conceptual framework of consolidation

2.1 What is consolidation?

The concept of financial consolidation is very simple. If two or more entities are under common control then they must be viewed as single entity - “**The Group**” - to obtain an overall financial picture of the group, as illustrated in Figure 1 below.

Figure 1: The concept of consolidation



This Guidance will address the issues of both how and why to consolidate.

2.2 Why consolidate?

The objective of consolidation is to provide a comprehensive financial picture of a group of entities as though they were a single entity. This is achieved by calculating:

- The combined assets and liabilities of the Group
- The combined revenues, expenditures, cash and financing flows of the group

This objective is the same whether the Group is a commercial group of companies or a national government.

2.2.1 A commercial group

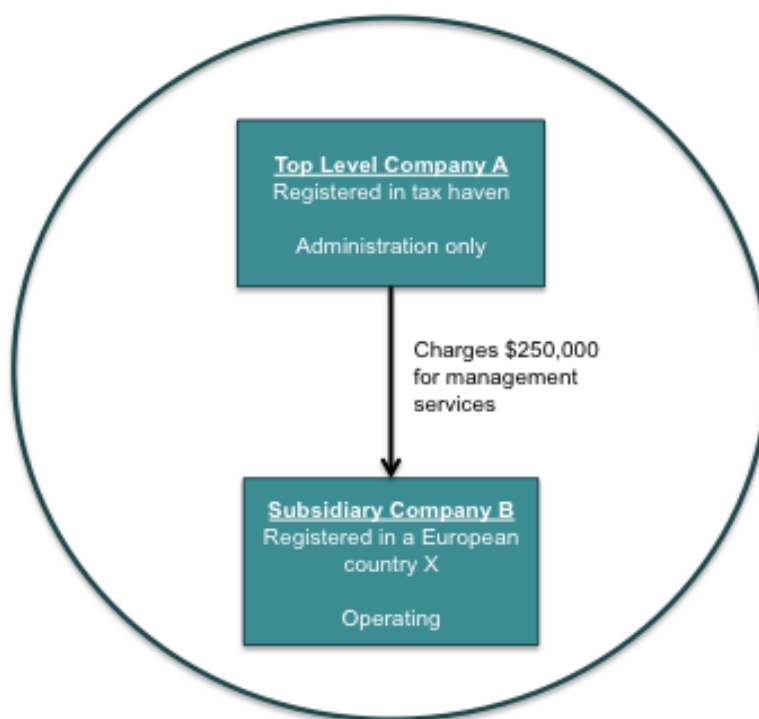
In the example of a commercial group of companies, consolidated information is important for investors, taxing authorities, employees and others with a financial interest in the Group. For example the Group may consist of two companies:

1. An operating company in a European country
2. A “top level” company in a tax haven.

The Group may seek to disguise its profits by making a very large management charge from the top-level company for management services.

Example 1: Example of commercial group

Some simple figures are used to illustrate this below.



In the above example suppose:

	<u>Individual companies</u>	<u>Consolidated</u>
Operating profit company B	\$350,000	<u>\$350,000</u>
Less: Management charge from A	<u>\$250,000</u>	

Reported profit in European country X	<u>\$100,000</u>	
Reported profit in tax haven	<u>\$250,000</u>	
Group profit		<u>\$350,000</u>

In the above example the Group has “moved” profit from European country X to a tax haven where the Group pays little or no tax. In fact this is exactly what many large multinational companies do in order to minimise their tax bill.

The consolidated information indicates correct profitability of the Group. Internal transfers are ignored.

2.2.2 A national government

Consolidated information on a national government will provide a comprehensive financial picture of the activities of the Government of the country. In many cases those activities will be conducted by a combination of central government, various legal entities under the national government and also by sub-national levels of government. Financial information on central government alone may not provide a comprehensive picture of the overall activities of the government. A simple example illustrates this point.

Example 2: Country X consolidation

A small Country X has just one legal entity operating under government - a hospital. Fees charged to patients fund the hospital. The following information applies:

	Central Government	Hospital	Consolidated
Health expenditure	\$100,000	\$800,000	\$900,000
Other expenditure	<u>\$4,900,000</u>	-	<u>\$4,900,000</u>
Total expenditure	<u>\$5,000,000</u>	<u>\$800,000</u>	<u>\$5,800,000</u>
Health expenditure as % total expenditure	2%	100%	15.5%

In this example only looking at central government indicates 2% of government expenditure is on health, whereas in fact total health expenditure is in excess of 15%. Only by looking at the consolidated information is it possible to obtain a comprehensive picture of government activity and expenditure.

2.2.3 Conclusions on why consolidate

From the above examples it is apparent that where there exists a Group of entities consolidated information is required to provide a comprehensive financial picture. In the public sector consolidation provides transparency and enables accountability.

However, it is also important to provide information on the individual entities within the consolidation. In the above example financial information is required on the hospital as a separate entity for the purposes of providing information both internally and to external stakeholders on the operation of the hospital.

Box 1: Consolidation - overview

Consolidation provides a high level financial overview of a group of entities
But
 Consolidation loses financial information on individual entities within the consolidation

2.3 How do you consolidate?

The process of consolidation is in principle very simple and consists of just two steps as summarised in Box 2 below.

Box 2: The universal process of consolidation

Step 1 Add together the financial information for all entities line by line for each of the balance sheet, operating and cash flow statement
Step 2 Cancel out any flows or balances between entities within the Group
Step 3 Eliminate any minority ownership of controlled entities

These three steps apply universally to all consolidations, whether in the commercial or public sector.

The example below provides a simple example of the consolidation process for a Government with just one wholly owned subsidiary organisation for the Operating Statement and Balance Sheet.

Example 3: Consolidation process (all figures in \$ million)

Description	National Government	Hospital	Aggregated (Step 1)	Flows/balances between entities	Consolidated (Step 2)
Operating Statement					
Revenue					
Tax revenue	125		125		125
Other revenue	30	25	55		55
Grant received		15	15	15	0
Total revenue	155	40	195	15	180
Expenditure					
Social services	50		50		50
Health	10	35	45		45
Education	40		40		40
Other	30		30		30
Grant to hospital	15		15	15	
Total expenditure	145	35	180	15	165
Operating surplus/deficit	10	5	15	0	15

Description	National Government	Hospital	Aggregated (Step 1)	Flows/ balances between entities	Consolidated (Step 2)
Balance Sheet					
Fixed (capital) assets					
Property and equipment	200	60	260		260
Financial assets					
Loan to hospital	50		50	50	0
Other	75		75		75
Total assets	325	60	385	50	335
Liabilities					
Loans	80		80		80
Loan from central government		50	50	50	0
Total liabilities	80	50	130	50	80
Net assets	245	10	255	0	255

The important principle of consolidation (as distinct from aggregation) is the need to eliminate flows and balances between entities in the Group. This elimination process is fundamental to the concept of consolidation.

This example does not include Step 3 as the Hospital is wholly owned by the national government (no external minority ownership). The methodology involving Step 3 is further explained in Section 6 “Methodology of Consolidation in the Public Sector”.

The logic for such intra-group elimination is that the flows and balances are internal when considering the Group as a whole. An analogy is an individual who moves an object from his left to his right hand - from the perspective of anyone else the individual is still holding the object.

2.4 What do you consolidate?

The issue of what to consolidate is complex and is examined in more detail later in this Guidance Note in Section 4 under the heading “Definition of The Entity to be Consolidated”. As a general principle financial consolidation takes place where there exists a group of entities that for a particular purpose should be considered as a single entity - usually referred to as Group.

2.4.1 Approaches to determining what entities should be consolidated

The four major approaches to defining the entities within a Group to be consolidated are as follows:

Legal

The Group is defined by law, e.g.

- Where one company owns the shares (equity) in another company together the two companies constitute a group
- Where an agency is created by law for public policy purposes and the law defines that agency as being under the control of Ministry

Sector	Particularly relevant to government structures, e.g. All of the entities within the General Government Sector may be regarded as a group and hence consolidated. When sector definition is set by the law it looks like the Legal approach.
Control	Control may exist even where there is no organisational relationship or ownership, e.g. If a Government Ministry by law appoints the Board of Directors of a company it effectively controls that company even if it does not own the company
Budget	In the public sector, another possible definition of the entities to be consolidated is all those entities that are included in the Government budget.

Establishing what entities should be consolidated for the purposes of Government financial reporting can raise issues that extend beyond the area of financial management. It is very often not easy to determine which entities are owned and/or controlled by government.

The two major international standards - International Public Sector Accounting Standards (IPSAS) and the IMF Government Finance Statistics Manual (GFSM) have adopted broadly consistent approaches to consolidation. However the two standards have different goals (as recognised in IPSAS 35) and in consequence have adopted different approaches to defining the entity to be consolidated. In the public sector the issue of what to consolidate is very important and will be considered in more detail in Section 3 below.

2.4.2 Conclusions on what to consolidate - the consolidation architecture

The issue of what to consolidate is complex and there are different approaches. As indicated these different approaches are examined in more detail in Section 4.

2.5 What is the end product of consolidation?

The end products of consolidation are reports. The different categories of reports are summarised as follows:

1. Consolidated budget documents
2. Consolidated financial reports for external users:
 - a. Audited financial statements
 - b. Statistical reports required by external users - GFS 2014 reports and also for members of the European Union reports in compliance with ESA 2008.
 - c. Interim and special reports, e.g. budget execution
3. Consolidated financial reports for management (not published)

It is important that the same procedures as described in Box 2 are applied to all consolidated reports. This will ensure consistency of the information that is provided.

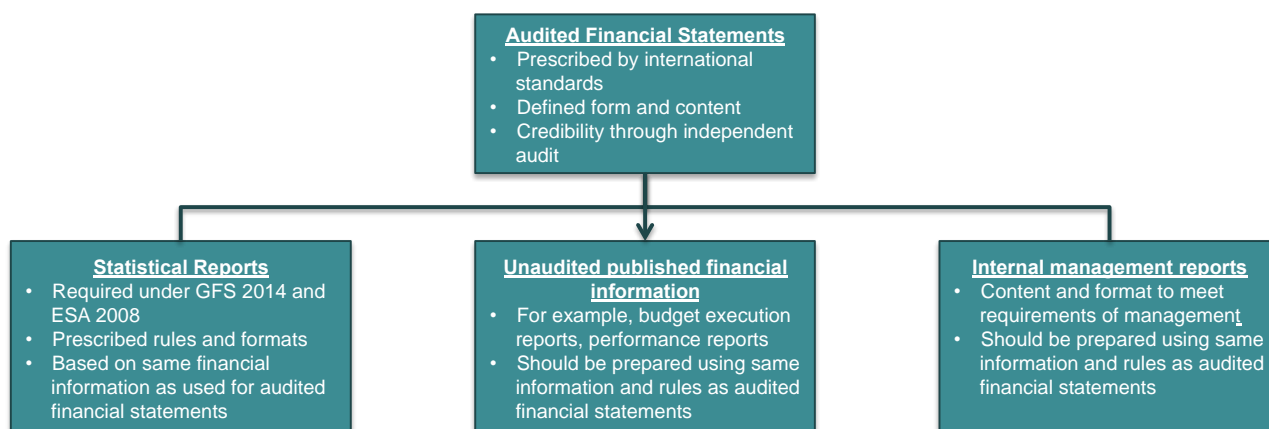
2.5.1 Audited Consolidated Financial Statements

This Guidance places particular emphasis on published audit consolidated financial statements. The reasons for this emphasis is as follows:

- International Standards (IPSAS) govern financial statements
- The statements are subject to independent audit and therefore have a higher level of credibility than other reports
- Financial statements should be the primary tools of transparency and accountability.

Using this approach the audited financial statements of the government should be seen as the top of a pyramid of financial reports, defining the methodology and information base for other reports, as illustrated in Figure 2 below.

Figure 2: Audit financial statements as the reporting pinnacle



Reporting is considered in more detail later in the Guidance Note.

2.6 What are the arguments for and against consolidation?

There are arguments both for and against consolidation, and circumstances under which consolidation is not appropriate. These are summarised below.

2.6.1 Arguments for consolidation

Consolidation enables an overall financial picture to be obtained of a group of entities. There is no other approach to obtaining such an overall picture.

- In the case of national governments consolidation provides a comprehensive view of the total government revenues, expenditures, financing, assets and liabilities.

- If the consolidation is carried out properly governments are prevented from hiding certain expenditures by creating separate entities to hide such expenditures, e.g. off balance sheet funding
- It enables comparability between different governments even though these may have different organisational structures, e.g. some countries may conduct all activities directly through the government, other countries may make extensive use of legal entities under the government
- Presents a comprehensive picture of liabilities and assets, including contingent liabilities

2.6.2 Arguments against consolidation

There are no conceptual arguments against consolidation, but a number of factors may make it infeasible or inappropriate in certain situations:

- Gathering the information for consolidation can be difficult, especially when there are a large number of subsidiary entities. In some cases reliance must be placed on unaudited information. In other cases an independent management of the subsidiary entity may resist providing information.
- The consolidation process can be complex and technically demanding, costing time and money, and using scarce resources.
- Political or other reasons may result in certain key entities not being consolidated thereby reducing the benefit of consolidated information.
- Consolidation can be meaningless where different entities use different accounting bases or policies.
- The consolidated information, though interesting, may not yield sufficient benefits to justify the cost and resources employed to gather the information.
- Consolidation provides a high level overview but in so doing loses detailed information on individual entities.
- In some non-market economies the consolidated government entity may be close to the whole economy and hence consolidation financial reports will have lost most of the information on flows within the economy.

2.6.3 Where consolidation is inappropriate

There are a number of situations where consolidation is inappropriate. IPSAS 35 provides a number of exceptions, but more generally the following may apply.

- Consolidation is inappropriate for national income accounts. Consolidation is not used in either the UN System of National Accounts (SNA) or the European System of Accounts (ESA), the two major national income statistical systems. This is because such statistical systems require information on transactions between entities within the economy. However, both SNA and ESA have methodologies to avoid double counting (see the separate section on ESA).

- Consolidation may be inappropriate where there are special circumstances. These are discussed in more details in Section 7 on exceptions from consolidation.

2.6.4 Conclusions on the arguments for consolidation

Consolidation is an important reporting tool. Consolidation provides high-level overview information that is not otherwise available. By doing so consolidation enhances transparency and accountability.

On the other hand there are situations where consolidated information may be inappropriate, infeasible or too costly to produce in comparison to the benefits. Each case must be considered on its merits.

Consolidation should never be seen as a replacement for financial reporting on the individual entity. Consolidation is an addition to such reports, not a replacement.

3 International Standards and Guidance on Consolidation

3.1 Overview

As indicated above, there are international standards for published financial statements and statistical reports. These standards include requirements for consolidation. Table 1 below summarises the existing standards and guidelines, their applicability and extent to which mandatory.

Table 1: International Standards for Consolidated Reports

Standard/ Guideline	Description	Applicability	Consolidation requirement	Are requirements mandatory?
Standards for entity financial reporting				
International Public Sector Accounting Standards (IPSAS)	A series of International standards for public sector financial reporting issued by the IPSAS Board of the International Federation of Accountants	Applicable to all General Purpose Financial Statements issued by public sector entities (other than Government Business Enterprises (GBEs))	Consolidation required	Not mandatory Individual countries must decide whether and how to apply IPSAS Adoption encouraged by international agencies
International Financial Reporting Standards (IFRS)	A series of international financial reporting standards issued by the IFRS Board	Applicable to entities other than public sector entities (but including GBEs). Most major stock exchanges require reporting by commercial entities in compliance with IFRS	Consolidation required	Only mandatory for entities whose shares are traded on a stock exchange that requires IFRS reporting or if required by the law of an individual country. But some countries have decided to apply IFRS to all public sector entities and in some countries to businesses not listed on a stock exchange
Standards for statistical reporting				
UN System of National Accounts (SNA) 2008	The UN statistical system for providing a standardised reporting system on national income and other aggregate national statistical measures	Statistical reports prepared and submitted by individual countries to provide macro level information on each country and for comparison between countries	Consolidation not required	Not mandatory but universally accepted and provides many of the rules and definitions used in GFS and ESA

Standard/ Guideline	Description	Applicability	Consolidation requirement	Are requirements mandatory?
IMF Government Finance Statistics (GFS) 2014	The GFS Manual (GFSM) sets out the requirement for statistical reports to the IMF on the public sector. GFS is consistent with SNA. The primary purpose of the GFS is to provide a comprehensive conceptual and reporting framework suitable for analyzing and evaluating fiscal policy, especially the performance of the general government sector and the broader public sector of any economy.	Applies to statistical reports submitted to the IMF. Besides, The harmonization of the GFS framework with other macroeconomic datasets means that data from GFS can be utilized as source data, or can be combined with data from other datasets to assess general government or public sector developments in relation to the rest of the economy	Consolidation required	If a country submits statistical reports to the IMF the GFSM is mandatory
European System of Accounts (ESA) 2010	A statistical reporting system for countries within the European Union (EU) based on the UN System of National Accounts (SNA)	Applicable to statistical reports submitted by EU member countries to the European Commission ESA reports are used to determine compliance with fiscal requirements of countries that have adopted the Euro	Consolidation not required	Mandatory under the Maastricht Treaty for all EU members

Note: there is ongoing discussion about the development of European Public Sector Accounting Standards (EPSAS) based on IPSAS that would be mandatory for members of the EU. However, at present such standards are only under discussion and the EU has made no decision on the introduction of EPSAS.

The requirements in Table 1 above can be summarised as follows:

- Consolidated financial reporting is required under all of IPSAS, IFRS and GFSM
- Consolidation is not required for statistical reports under SNA or ESA

Furthermore the basic principles of consolidation are the same across all of IPSAS, IFRS and GFSM. However, there are differences between these sets of standards about what to consolidate. Also IPSAS and IFRS provide more detailed guidance on situations such as partial ownership and joint ventures than is provided by GFSM.

This also means that a common database of accounting information can be used for all consolidation purposes. This Guidance Note does not address the issues of differences between the valuation methodology prescribed in IPSAS, IFRS and GFSM.

The next two sub-sections provide more detailed information on the consolidation requirements of IPSAS and GFSM. The IFRS requirements are the same as IPSAS (in fact the IPSAS requirements are derived from IFRS). The UN SNA and EU ESA are not considered in detail as they do not require consolidation.

3.2 GFSM consolidation requirements

Government Finance Statistics (GFS) is the standardised reporting system developed and managed by the IMF. *“The GFS framework is designed to provide statistics that enable policymakers and analysts to study developments in the financial operations and financial position of government. GFS also allow an assessment of the liquidity and sustainability of the finances of the general government sector or the public sector in a consistent and systematic manner. The GFS framework can be used to analyze the operations of a specific level of government, transactions between levels of government, and the public sector”* (GFSM 2014 Para 1.10)

GFS is based on the UN System of National Accounts (SNA) and definitions used in the GFS are consistent with SNA definitions. GFS is based on generally accepted concepts including the requirement to consolidate information.

The GFS Manual (GFSM) describes the system and is applied by countries in preparing GFS reports. The latest edition is 2014 (currently this is described as “pre-publication but no substantive changes are expected. GFSM 2014 is consistent with SNA 2008. It is based on accrual accounting principles (though applied somewhat differently to IPSAS).

The basic principles of consolidation as described in GFSM 2014 are identical to those in IPSAS and also as described in Section 2.1 above.

Box 3: GFS definition of consolidation

Consolidation is a method of presenting statistics for a set of units (or entities) as if they constituted a single unit (GFSM 2014 Para 3.153)

The architecture of consolidation in GFS is based on economic sectors rather than on concepts of control. This is considered further below in Section 4. This approach to consolidation means that many of the complications of IPSAS simply do not occur.

The methodology of consolidation is also as for IPSAS and described in Box 2. However, there are conceptual and practical variations in GFSM 2014.

Conceptual

Social security and taxes deducted from employees and paid to other agencies of government are both treated as being paid to the employee as part of his or her remuneration, and then by the employee to the relevant government fund or agency. This is consistent with the IPSAS approach.

Practical

Flows between economic units are only eliminated if they are significant. The following rule is suggested in GFSM 2014

Box 4: One sided rule of thumb on determining if flows between entities are significant

The “one-side” rule of thumb is commonly used. That is, if there is convincing evidence from the one institutional unit that a flow or stock position exists, it should be imputed to the counterparty. The imputation should be recorded even if there is no record of the flow or stock position in the counterparty’s accounts. When such an adjustment is made in the data for a unit where the flow or stock position cannot be directly identified, it will be necessary to ensure that the records for that unit are properly modified. (GFSM 2014 Para 3.165)

There are no disclosure requirements in GFSM 2014 for narrative information on consolidated entities. GFS reports are exclusively a series of numeric reports (see Section 8).

3.3 IPSAS consolidation requirements

As indicated above IPSAS are issued by the IPSAS Board of IFAC. Though this is a private organisation, the standards are supported by most major multilateral organisations, including the IMF, World Bank, UN and EU (although IPSAS are not mandatory for EU member countries).

The IPSAS relating to consolidation were updated in 2015 and the previous IPSAS 6, 7 and 8 have been withdrawn. The IPSAS currently in issue and relevant to consolidation are as follows:

IPSAS 22	Disclosure of Financial Information about the General Government Sector
IPSAS 34	Separate Financial Statements
IPSAS 35	Consolidated Financial Statements (replaces IPSAS 6)
IPSAS 36	Investment in associates and Joint Ventures (replaces IPSAS 7)
IPSAS 37	Joint arrangements (replaces IPSAS 8)
IPSAS 38	Disclosure of Interest in Other Entities
Cash Basis IPSAS	Requires countries reporting under the cash basis to consolidate controlled entities.

Each of the above IPSAS is briefly summarised below. Detailed requirements are examined in the appropriate section of this Guidance Note.

IPSAS 22 Disclosure of Financial Information about the General Government Sector

IPSAS 22 allows (but does not make mandatory) consolidated financial reports to include statements consolidating the General Government Sector (GGS) as defined in the UN SNA and GFSM. Statements consolidating the GGS will be additional to consolidated financial statements prepared in accordance with IPSAS 35.

The consolidated GGS statements should record Public Corporations (Financial and Non-financial) as investments. Thus the GGS financial statements are an additional financial report included within the overall financial reports of the entity. The GGS consolidated financial statements must be reconciled with the financial statements prepared in accordance with IPSAS 35.

IPSAS 34 Separate Financial Statements

Applicability

IPSAS 34 applies where an entity has investments in other controlled entities and such investments are not consolidated. There could be one of two reasons why this could be the case:

1. The top level entity is an investment entity (e.g. a sovereign wealth fund) that is exempted from the requirements to consolidate, or
2. The top level entity is stopped by law from consolidating certain entities, or

IPSAS 34 sets out the requirements for separate financial statements and the valuation of investments. Since these are not consolidated accounts IPSAS 34 is not directly relevant to this Guidance Note and is not further considered.

IPSAS 35 Consolidated Financial Statements

IPSAS 35 is now the main IPSAS relevant to consolidated financial reporting as it replaces IPSAS 6. IPSAS 35 requires that any public sector entity (other than GBEs) shall prepare consolidated financial statements. The only exceptions are intermediate controlling entities within a hierarchy of consolidation (see Figure 8 above) and investment entities (e.g. wealth funds). The exceptions are considered in more detail in Section 7 below. The definition of control is considered in Section 4 below.

Consolidated financial statements are defined as *“the financial statements of an economic entity in which the assets, liabilities, net assets/equity, revenue, expenses and cash flows of the controlling entity and its controlled entities are presented as those of a single economic entity.”* This is in accordance with the illustration in Example 3 above. The consolidation process required under IPSAS 35 is as described in Box 2 above.

The additional requirements of IPSAS 35 not covered elsewhere in this Guidance Note are:

- Financial policies of all entities in the Group should as far as possible be uniform. If they are not uniform then adjustments should be made so that all information is based on the same accounting policies.
- All the consolidated entities should have the same financial period end. If this is not the case use the most recent financial statements of the controlled entity and adjust for transactions up to the end of the financial period of the top-level entity.

IPSAS 36 Investment in associates and Joint Ventures

IPSAS 36 extends the concept of consolidation to associates and joint ventures. It applies where the top-level entity has “significant influence over, or joint control of, an investee [i.e. another entity] where the investment [in the investee] leads to the holding of a quantifiable ownership interest.” Significant interest is defined as: “*the power to participate in the financial and operating policy decisions of another entity but [significant interest] is not control or joint control of those policies.*”

IPSAS 36 applies to associate and joint ventures there is a quantifiable interest, e.g. ownership of shares. As a general rule if an entity holds a quantifiable ownership interest in another entity of 20 per cent or more of the voting power of the investee, then it is presumed that the entity has significant influence.

Where IPSAS 36 applies, then the investment in the other entity is valued using the equity method. Under this approach the total value of the investee is the net asset value of that entity according to the financial statements of the investee. The portion owned by the top level entity is recorded as a non-current asset.

Example 4: Valuation of investment in an associate

The government of X owns 30% of the shares of Company Z. It is therefore treated as an associate and accounted for using the equity method. Suppose the net asset value of Company Z is \$500,000. The value of the portion owned by Government X is therefore \$150,000 and this amount is shown in the financial statements of X as a non-current asset.

If the financial period end of Company Z is different to Government X then the same procedures as above for consolidation under IPSAS 35 apply.

The application of IPSAS 36 will be difficult for non-business investments where there may be no shares and therefore it may be difficult to determine the portion of the entity owned by the top-level entity.

IPSAS 37 Joint Arrangements

Applies to situations where the top-level entity is in some form of joint arrangement over another entity. A joint arrangement is an arrangement of which two or more parties have joint control. Joint control is the agreed sharing of control of an arrangement by way of a binding arrangement, which exists only when decisions about the relevant activities require the unanimous consent of the parties sharing control.

Joint control is the sharing of control of an arrangement, which exists only when decisions about the relevant activities require the unanimous consent of the parties sharing control. The sharing of control may have been agreed by way of a binding arrangement.

If an entity is in a joint arrangement then it must decide whether there exists collective control of the entities by all of the parties involved. All the parties control the joint arrangement collectively when they must act together to direct the activities that significantly affect the benefits from the arrangement.

A joint arrangement has the following characteristics:

1. The parties are bound by a binding arrangement
2. The binding arrangement gives two or more of those parties joint control of the arrangement.

A joint arrangement is either a joint operation or a joint venture.

- A joint arrangement is an arrangement of which two or more parties have joint control.
- A joint venture is a joint arrangement whereby the parties that have joint control of the arrangement have rights to the net assets of the arrangement.

The classification of a joint arrangement as a joint operation or a joint venture depends upon the rights and obligations of the parties to the arrangement, as described above. The accounting treatment in the joint operator (i.e. the top level company) depends on whether it is a joint operation or a joint venture.

The accounting arrangements are summarised in Table 9 below.

Table 2: Accounting for joint operations and joint ventures

Investment as shown in financial statements of joint operator	
Joint operation - what part of joint arrangement entity is included in financial statements of top level entity	Joint venture
Assets, including share of assets held jointly	Accounted for using the equity method as described in IPSAS 36 (see above)
Liabilities, including share of liabilities incurred jointly	
Revenue including revenue from the sale of its share of the output of the joint operation	
Share of the revenue from the sale of the output by the joint operation	
Expenses including its share of any expenses incurred jointly	

IPSAS 38 Disclosure of Interest in Other Entities

IPSAS 38 applies to all of the situations described in IPSAS 35, 36 and 37, and extends the disclosure requirements. The stated objectives of IPSAS 38 are to require an entity to disclose information that enables users of its financial statements to evaluate:

- (a) The nature of, and risks associated with, its interests in controlled entities, unconsolidated controlled entities, joint arrangements and associates, and structured entities that are not consolidated; and
- (b) The effects of those interests on its financial position, financial performance and cash flows. IPSAS 38 applies to any entity that has any entity that has:
 - i. Controlled entities;
 - ii. Joint arrangements (i.e., joint operations or joint ventures);
 - iii. Associates; or
 - iv. Structured entities that are not consolidated

The definition of structured entities is complex and requires detailed study of the IPSAS by any country where it may be relevant. More information is provided in Annex 4.

Disclosure requirements

IPSAS 38 contains extensive disclosure requirements in all of the above situations.

The significant judgments and assumptions it has made in determining:

- (a) The nature of its interest in another entity or arrangement;
 - i. The type of joint arrangement in which it has an interest (paragraphs 12–14); and
 - ii. That it meets the definition of an investment entity, if applicable (paragraph 15); and
- (b) Information about its interests in:
 - i. Controlled entities (paragraphs 17–26);
 - ii. Joint arrangements and associates (paragraphs 35–39);
 - iii. Structured entities that are not consolidated (paragraphs 40–48);
 - iv. Non-quantifiable ownership interests (paragraphs 49–50); and
 - v. Controlling interests acquired with the intention of disposal (paragraphs 51–57).

Furthermore, as an all embracing requirement, if all of the disclosures under this or any other standards do not meet the objective of IPSAS 38 as described above, then an entity shall disclose whatever additional information is necessary to meet that objective.

Each reporting entity is allowed discretion on the level of detail to be disclosed: “An entity shall consider the level of detail necessary to satisfy the disclosure objective in paragraph 1 and how much emphasis to place on each of the requirements in this Standard. It shall aggregate or disaggregate disclosures so

that useful information is not obscured by either the inclusion of a large amount of insignificant detail or the aggregation of items that have different characteristics

An entity shall disclose the methodology used to determine:

- (a) That it has control of another entity as described in paragraphs 18 and 20 of IPSAS 35;
- (b) That it has joint control of an arrangement or significant influence over another entity; and
- (c) The type of joint arrangement (i.e., joint operation or joint venture) when the arrangement has been structured through a separate vehicle.

An entity shall disclose information that enables users of its consolidated financial statements:

- (a) To understand:
 - i. The composition of the economic entity; and
 - ii. The interest that non-controlling interests have in the economic entity's activities and cash flows (paragraph 19); and
- (b) To evaluate:
 - i. The nature and extent of significant restrictions on its ability to access or use assets, and settle liabilities, of the economic entity (paragraph 20);
 - ii. The nature of, and changes in, the risks associated with its interests in consolidated structured entities (paragraphs 21–24);
 - iii. The consequences of changes in its ownership interest in a controlled entity that do not result in a loss of control (paragraph 25); and
 - iv. The consequences of losing control of a controlled entity during the reporting period (paragraph 26).

When the financial statements of a controlled entity used in the preparation of consolidated financial statements are as of a date or for a period that is different from that of the consolidated financial statements (see paragraph 46 of IPSAS 35) an entity shall disclose:

- (a) The date of the end of the reporting period of the financial statements of that controlled entity; and
- (b) The reason for using a different date or period.

Information is also required on the interest of other entities in any entities controlled by the top-level entry (in effect the other side of the IPSAS 36 and 37 disclosures). Detailed requirements are in the IPSAS Paras 19 through 26. As they only apply in limited situations they are not repeated in this Guidance Note.

Finally there are disclosure requirements in a number of special situations:

- Interest in unconsolidated entities (Paras 27 - 34)
- Interest in joint arrangements and associates (Paras 35 - 39)

- Interests in structured entities not consolidated (Paras 40 - 48)
- Non-quantifiable ownership interests (Paras 29 - 56)

In total IPSAS 38 provides very extensive disclosure requirements of all the interests and risks of a top level reporting entity, e.g. national government. The IPSAS requires very detailed study to ensure full compliance.

Cash Basis IPSAS

The Cash Basis IPSAS also contains consolidation requirements for countries reporting under the Cash Basis. These requirements are based on IPSAS 6 (not yet updated to IPSAS 35). The main provisions are exactly as IPSAS 35:

- Consolidation of all controlled entities
- Same consolidation methodology

The disclosure requirements are more limited and are described in

Box 5: Cash Basis IPSAS consolidation disclosure requirements

An entity shall disclose the following information in the notes in respect of each controlled entity referred to in paragraph 51:

- (a) The name of the controlled entity and a description of its key activities;
- (b) The rationale for the acquisition of the controlling interest and the factors considered in determining that control exists;
- (c) The impact on the consolidated financial statements of consolidating the controlled entity including the effect on assets, liabilities, revenue, expenses and net assets/equity; and
- (d) The current status of the approach to disposal, including the expected method and timing of disposal.

However, it should be noted that the IPSAS Board is currently considering revisions to the Cash Basis IPSAS. One change being considered for simplification is the consolidation requirements.

Conclusions on IPSAS and consolidation

In total the IPSAS contain extensive, complex and detailed requirements for consolidation including disclosure requirements and the provision of information in situations where control does not exist but there is significant influence.

Only a few countries that have fully adopted accrual accounting and are committed to reporting in compliance with IPSAS. Therefore only these few countries are likely to be able to fully implement all of the requirements of the above IPSAS.

However, even when a country is not yet at the level of implementing all the IPSAS consolidation requirements, there should be an awareness of the requirements as an indication of good practice.

3.4 UN SNA 2008 and ESA 2010

Both the UN SNA 2008 and ESA 2010 state that as a matter of principle the statistics of institutional units should not be consolidated in the national accounts. However consolidated accounts may be compiled for complementary presentations and analyses. Even then, transactions appearing in different accounts of the national accounts are never consolidated. The difference between, on the one hand, SNA 2008 and the ESA 2010, and on the other hand IPSAS and GFSM 2014 reflects the different uses of financial information. The GFS framework is designed to produce statistics suitable for use in the analysis of the net relations between government and the rest of the economy. The IPSAS framework is designed to provide financial information on groups of public sector entities under common control. The IPSAS and GFS frameworks are not intended to produce a measure of production. SNA 2008 and ESA 2010, on the other hand, serve a range of other uses, including a comprehensive measure of production and relations among all the sectors of the economy.

4 Definition of The Entity to be Consolidated

4.1 The concept of the consolidation entity

This issue has already been introduced in Section 2.4 above. Four approaches to consolidation were considered. These four approaches are evaluated in Table 3 below

Table 3: Evaluation of approaches to defining the consolidation entity

Approach	Merits	Disadvantages	Conclusions
1. Legal	Simplicity since explicit in law	In many jurisdictions no legal requirement for consolidation Not consistent between countries so inter country comparisons not possible	If there is a legal requirement to consolidate certain entities that requirement must be complied with But does not provide a general approach across different countries
2. Budget	Ensures consistency with the budget for budget monitoring	Some public sector entities not included within Government budget Not everything funded through the budget is part of the public sector Budget coverage varies between countries	Not suitable as general basis for consolidation
3. Control	Links to managerial responsibility concepts Principle of "substance over form" what a top level entity really controls	Concept of control can be difficult to apply Consolidation will not coincide with generally accepted definitions of the public sector Controlled entities will vary between countries restricting scope for international comparison	Basis of IPSAS consolidation - must be used to be IPSAS compliant Also part of GFS basis of defining entities within GGS and public corporation sector
4. Sector	Based on UN, GFS and ESA definitions of public sector (GGS and public corporations) Provides a consistent basis for reporting and international comparison	Does not link to concept of managerial control Not all entities within public sector will be controlled by central government	Part of basis for GFS consolidated reporting (Control also used in GFS to identify entities to be consolidated)

From the above it is apparent that the two generally used approaches to defining the consolidation entity are based on either control or sectors. It is also clear that the IMF GFS and IPSAS use different approaches, which may result in the consolidation of different groups.

The two approaches are examined below.

4.2 The GFS approach to determining the consolidation entity

4.2.1 General principle

The GFS definition of what to consolidate commences by stating a general principle:

Box 6: General principle applicable in deciding what entities to consolidate under GFS

GFS should cover all entities that materially affect fiscal policies. Normally, fiscal policies are carried out by entities, established by political processes, wholly devoted to the economic functions of government (GFSM 2014 Para 2.1)

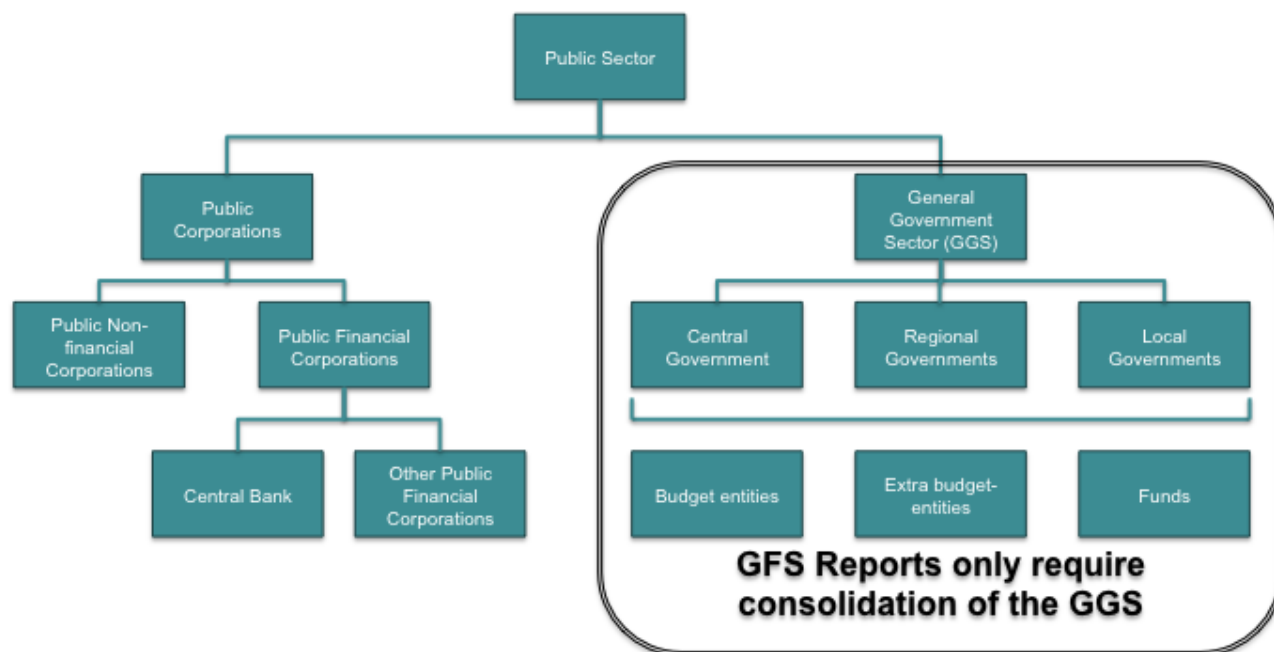
The whole of Chapter 2 of GFSM 2014 explains how the above principle is to be applied, and therefore defines what is to be consolidated. The following sub-sections provide an overview of the requirements.

4.2.2 Structure of the public sector

The IMF GFSM requires the consolidation of resident entities within the public sector. The IMF GFSM 2001 defines the parameters of the public sector and general government sector as illustrated in Figure 3 below.

Note that the required GFS Reports only require consolidation of the General Government Sector (see Section 8).

Figure 3: Structure of the Public Sector



Notes:

1. Illustration based on GFSM 2014

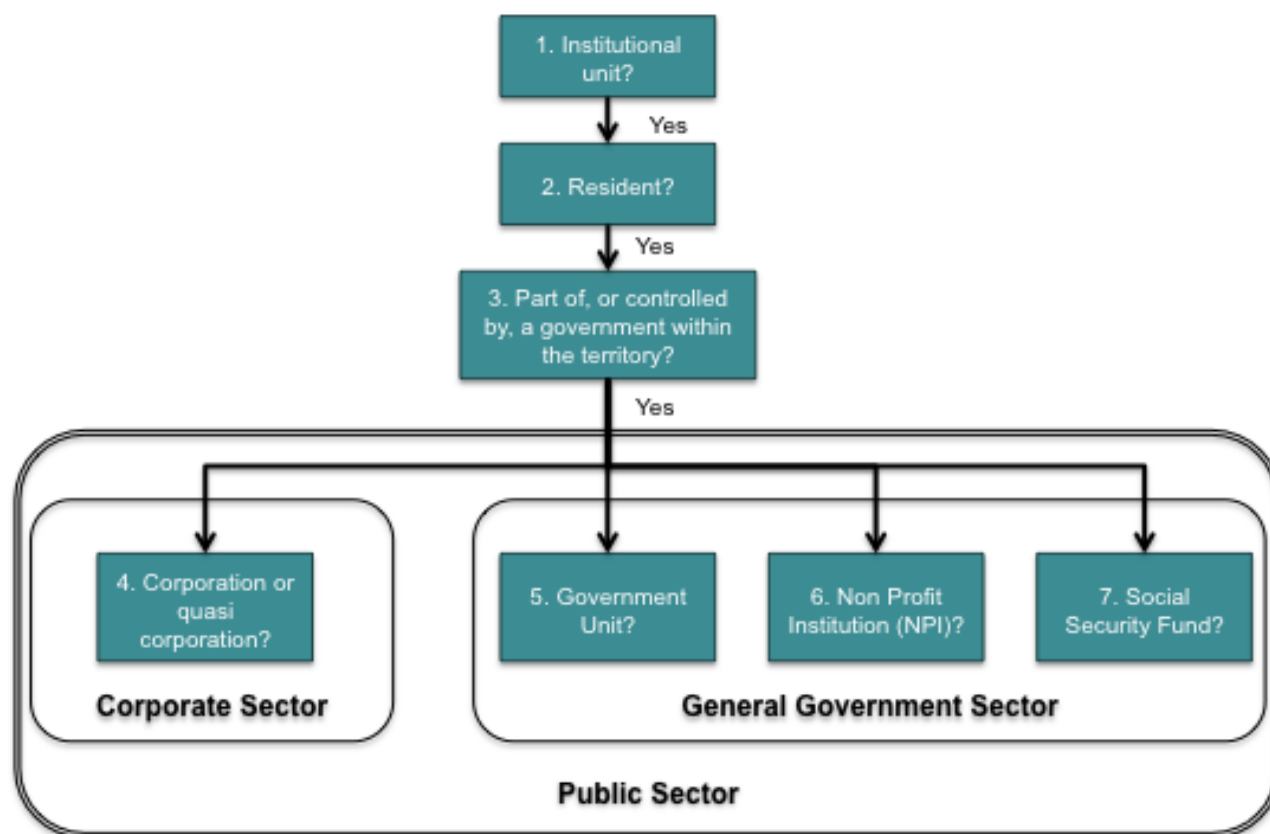
2. The GFSM definition of Public Corporations is for practical purposes the same as the IPSAS definition of Government Business Enterprises (GBEs). However, IPSAS does not distinguish between financial and non-financial GBEs.

The GFS structure as illustrated in Figure 3 is consistent with the definition of the public sector structure in UN SNA and ESA 2010. It is the generally accepted structure of the public sector for statistical analysis.

4.2.3 Decision tree for GFS consolidation

In order to identify and categorise the entities to be included in the above structure there is a multi stage decision process for each entity. A simplified decision tree is shown in Figure 4 below, and then explained in the following sub-sections.

Figure 4: Simplified GFS decision tree



Note: this is a simplified version of the decision tree in GFSM 2014 Figure 2.4

1. Institutional unit

“An institutional unit is an economic entity that is capable, in its own right, of owning assets, incurring liabilities, and engaging in economic activities and in transactions with other entities” (GFSM 2014 Para 2.22). It is only possible to consolidate institutional units. If an activity does not qualify as an institutional unit then the institution unit to which that activity belongs must be identified.

2. Resident

Only resident institutional units will be included in the public sector for consolidation and reporting. Residence is determined by the economic territory (i.e. country) with which the institutional unit has the strongest connection.

The term “territory” is used in GFSM 2014 rather than “country” though these two terms will usually be synonymous. However, in some cases the definition of territory will not be simple. Examples include disputed territories and regions. These are political issues and the decision on what to consolidate also becomes a political decision. Territory also includes enclaves with other countries, e.g. embassies.

A particular case is so-called “Special Purpose Entities” (SPEs). SPEs are also sometimes referred to as “brass plate companies” or “shell companies”. SPEs are entities which have little or no physical presence in the territory in which they are legally constituted or legally domiciled (e.g., registered or licensed). The substantive activities of the SPE are conducted in a different territory. In such circumstances, residence of the SPE is attributed to the territory in which the SPE is legally constituted or domiciled. However, the fiscal activities of non-resident government-controlled SPEs should be reflected in GFS as part of the public sector (GFSM 2014 Para 2.15).

Note that there is no residency requirement when deciding which units to consolidate under IPSAS. This is a fundamental difference. The requirement for residency flows from the general principle underlying GFS as set out in Box 6 above.

3. Part of, or controlled by, a government within the territory

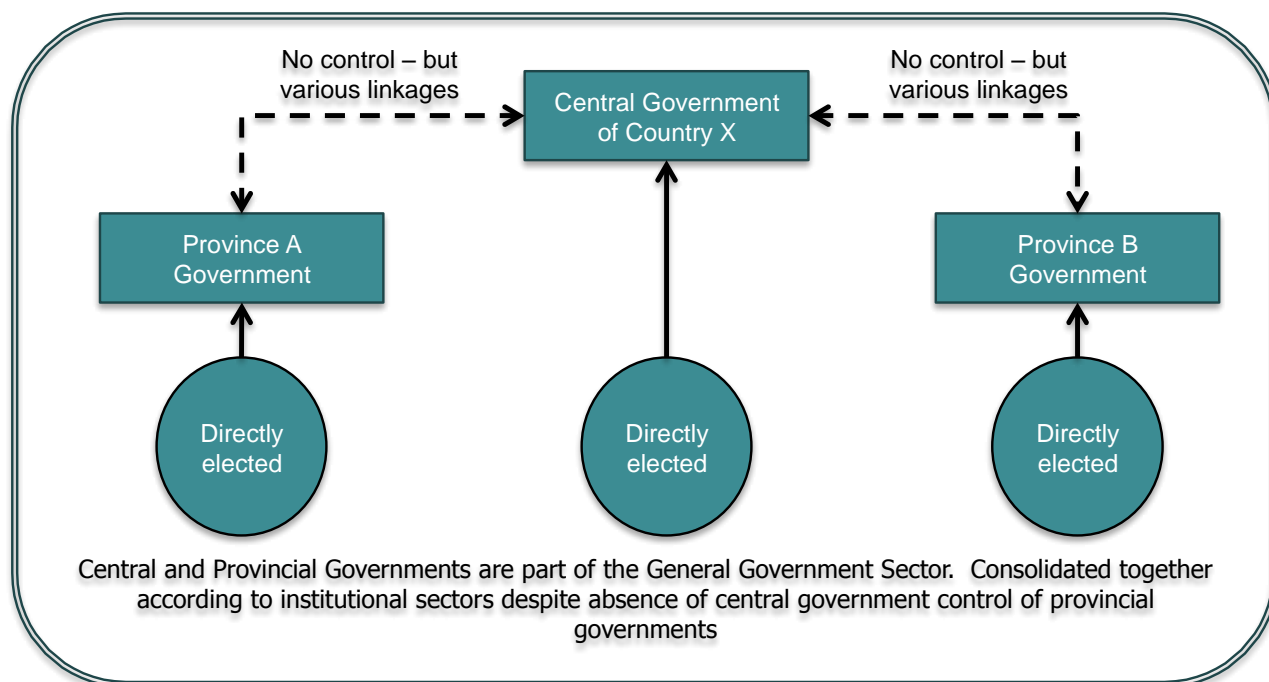
To be part of the public sector an institutional unit must be either:

1. Part of a government within the territory (= country), OR
2. Controlled by such a government within the territory.

A government means any of central government, provincial government, state government, regional government, local government and also social security funds.

In many countries sub-national levels of government are not “controlled” by central government. For example, a regional government may be directly elected and have an independent responsibility to the citizens of that region. For GFS this lack of control does not matter - government controlled entities are consolidated together even though the governments themselves are not centrally controlled. This is illustrated in Figure 5 below.

Figure 5: Effect of sub-national governments not being controlled by central government



Entities that are part of, or controlled by, a government (Central or Provincial) are all part of the public sector. Such entities are sub-classified into categories:

- Corporations and quasi corporation together comprise the Corporate Sector
- Government units, NPIS and social security funds together form the General Government Sector (GGS).

Before classifying such entities it is necessary to determine if the entity is controlled by a government. The indicators for Corporations and NPIS are summarised in Table 4 below.

Table 4: Determining if control exists over corporations and NPIS

Corporation	Not For Profit Institution (NPI)
Control of a corporation is defined as the ability to determine the general corporate policy of the corporation. To determine if a corporation is controlled by the government, the following eight indicators of control would be the most important and likely factors to consider	Control of an NPI is defined as the ability to determine the general policy or program of the NPI. To determine if an NPI is controlled by the government, the following five indicators of control would be the most important and likely factors to consider:
1. Ownership of the majority of the voting interest (aggregate ownership by different government entities)	1. The appointment of officers.
2. Control of the board or other governing body	2. Other provisions of the enabling instrument (law, decree or regulation)
3. Control of the appointment and removal of key personnel.	3. Contractual agreements

Corporation	Not For Profit Institution (NPI)
4. Control of key committees of the entity	4. Degree of financing by government
5. Golden shares and options.	5. Risk exposure
6. Regulation and control	
7. Control by a dominant public sector customer or group of public sector customers	
8. Control attached to borrowing from the government	

From Table 4 it is apparent that the rules for determining controls of both corporations and NPIs are very similar and based on common principles.

Joint ventures, joint control and partial ownership of entities

The Guidance and consolidation procedures in GFSM 2014 are much simpler than the detailed rules in IPSAS 36 and 37. According to GFSM 2014 any of the above is treated as either part of the public sector or the private sector according to the rules set out in the preceding sub-sections.

GFSM 2014 guidance is summarised as follows:

- Corporations - part of the public sector if controlled by government (more than 50% of equity)
- NPIs - part of the GGS if controlled by government.

Joint operating arrangements are not recognised as institutional units. Assets and revenues should be shared according to contractual arrangements.

As we have already stated above, to the public administration bodies are classified as institutional units, implementing public administration functions as their key responsibility. For example, the Ministry of Finance, the Ministry of Industry or municipal administrations are public sector units, as each of them implements the function of public administration.

4. Corporations and quasi corporations

The public corporations subsector consists of all resident corporations controlled by government units or by other public corporations. (GFSM 2014 Para 2.104)

Entities that are controlled by government and are market producers are classified as part of the Public Corporations sector. If an entity lacks legal status but meets the definition of an institutional unit and is also a market producer it is a quasi corporation and also included with the Public Corporations Sector. Definitions of market and non-market producers are provided in Box 7 below.

Note that this distinction is very important because of the need to separately consolidate the General Government Sector as distinct from the Corporation Sector.

Box 7: Definition of market and non-market producers

A market producer is an institutional unit that provides all or most of its output to others at prices that are economically significant. A nonmarket producer provides all or most of its output to others for free or at prices that are not economically significant.

Economically significant prices are prices that have a significant effect on the amounts that producers are willing to supply and on the amounts purchasers wish to buy. These prices normally result when:

- The producer has an incentive to adjust supply either with the goal of making a profit in the long run or, at a minimum, covering capital and other costs; and
- Consumers have the freedom to purchase or not purchase and make the choice on the basis of the prices charged.

(GFSM 2014 Para 2.65 and 2.66)

Corporations - legal entities, set up for the purpose of production of goods or services for the purpose of their sales on the market. Corporations can serve as a source of income or other financial benefit for all the co-owners. Corporations are in collective ownership of all shareholders, which have the right to appoint directors, responsible for overall management of the corporation. Institutional units, belonging to the public administration bodies or are under their control, which are classified as corporations in the above referred meaning, are called state-owned corporations (organizations) (GFSM 2001, par. 2.14).

Quasicorporations - these are entities, which are not corporations and are not set up in any other organisational form provided by the law, which function as a corporation. Quasi-corporations are considered as institutional units separate from those to which they are subordinated in accordance with the law.

Corporations and quasi corporations are sub-divided into:

- Nonfinancial corporations are corporations whose principal activity is the production of market goods or nonfinancial services (GFSM 2014 Para 2.114)
- Financial corporations are corporations that are principally engaged in providing financial services, including insurance and pension fund services, to other institutional units (GFSM 2014 Para 2.115).
- Financial corporations sector always includes the Central Bank even though it may be argued this is not a market producer (GFSM Para 2.117)

5. Government units

Government refers to central, state, local or any other sub-national government:

- **Central government** - the political authority of the central government extends over the entire territory of the country (GFSM 2014 Para 2.85)
- **State governments** - institutional units exercising some of the functions of government at a level below that of central government and above that of the government institutional units existing at a local level, e.g. state, region or provincial government (GFSM Para 2.90)

- **Local government** - institutional units whose fiscal, legislative, and executive authority extends over the smallest geographical areas distinguished for administrative and political purposes

The General Government Sector consists of all units of government and NPIs controlled by such units of government.

General government entities with budgets not fully covered by the general budget are considered extra budgetary (GFSM 2014 Para 2.82). Such extra budgetary units are treated as part of the GGS provided they operate under the authority or control of a central, state, or local government

6. Non Profit Institutions

Nonprofit institutions (NPIs) are legal or social entities created for the purpose of producing or distributing goods and services, but they cannot be a source of income, profit, or other financial gain for the institutional units that establish, control, or finance them (GFSM 2014 Para 2.36).

NPIs may be engaged in non-market production of goods or services, e.g. schools or hospitals charging small fees for additional services. However, if their production meets the criteria of market production then the NPI must be re-classified as a Public corporation. The definitions above of market producers, plus the further explanation in GFSM 2014, must be used to determine whether an entity should be classified as an NPI or as a public corporation.

NPIs controlled by government form part of the General Government Sector.

7. Social Security Funds

A social security fund is a particular kind of government unit that is devoted to the operation of one or more social security schemes (GFSM 2014 Para 2.100). Criteria to be included in this definition are:

- Organised and managed separately from the other activities of government units
- Holds assets and liabilities separately from other government units
- Engages in financial transactions on its own account.

Social Security Funds should be distinguished from Social Security Schemes, which cover the community as a whole, or large sections of the community, and are imposed and controlled by government units. Social insurance schemes provide social protection and require formal participation by the beneficiaries, evidenced by the payment of contributions (actual or imputed). A social security scheme may be either:

1. A Social Security Fund, or
2. A Public Corporation

The details of how the scheme is managed and operates will need to be examined to determine the appropriate classification.

It is usual to present social security funds in one of two alternative sets of subsectors:

- All social security funds could be combined into a separate GGS subsector and all other general government units could be classified according to their level. In that case, the central, state, and local government subsectors would comprise all government units other than social security funds; or
- Social security funds could be classified according to the level of government that organizes and manages them and therefore be combined with the other general government units at the respective subsectors. Thus, the general government would consist of central, state, and local governments, assuming that all three levels of government exist.

Example 5: Determining entity classification

The Government of country X has 100% ownership of an airline company called “Government Air”. The base of operations is within Country X, though the company has sales offices in other countries.

Question 1: Does Government Air belong to the public sector? Yes - it is a resident intutional unit controlled by government (the main base of operations is in Country X).

Question 2: is it a public corporation or part of the GGS? This depends on the nature of the activities of Government Air:

- It could be established by the Government for the purpose of providing transportation of exclusively to members of the Government. Financing of activities would be by granting subsidies and making capital payments for acquisition of aircraft. In this case it is an NPI and forms part of the GGS.
- Alternatively the Government for the purpose of developing the air transportation market could establish Government Air. This could be to challenge foreign airline companies which currently prevail. In this role Government Air could act as a market-based service provider, after receiving from the Government only certain statutory capital in the form of aircrafts, an office building and, possibly, some part of current assets. It would operate with the intention of making a profit by selling airline seats to the general public at market prices. In this case it would be classified as a non-financial public corporation.
- Finally Government Air could be established with a mixture of the above two objectives. In this case it will be necessary to examine the balance between the activities and facts such as the prices charged to government staff for flights in order to determine whether the entity should be classified as a Public Corporation or an NPI.

4.3 The IPSAS approach to determining the consolidation entity

The IPSAS criteria for determining entities to consolidate are based on the concept of control: “*An entity that is a controlling entity shall present consolidated financial statements*” (IPSAS 35 Para 5). Note that the concept of consolidation of sectors (as used in GFS) does not exist under IPSAS.

Note that the IPSAS approach is linked to the concept of managerial responsibility. It could be argued that this approach is more appropriate for establishing accountability.

A controlling entity is an entity that has one or more controlled entities:

- A controlled entity is an entity (including an unincorporated entity such as an investment partnership) which is under the control of another entity known as a controlling entity.
- The controlling entity and controlled entities determine group of entities, which in its turn could be a controlled entity for some other controlling entity.

The only exceptions to IPSAS 35 consolidation requirements are:

1. Intermediate controlling entities within a hierarchy of controlled entities
2. An investment that is required to measure all of its controlled entity through surplus or deficit.

The exceptions are explained in more detail in Section 7 below.

IPSAS 35 does not apply to GBEs. However, if a GBE is controlled by a public sector entity that is not a GBE, then IPSAS 35 applies to the consolidation of such controlled GBEs in the financial statements. This is very important because it means that IPSAS consolidated financial statements must include controlled GBEs (note the difference to GFS where GBEs are called Corporations and are not consolidated as part of the GGS).

The criteria under IPSAS for determining control are set out in Box 8 below.

Box 8: IPSAS criteria for control

An entity controls another entity when it is exposed, or has rights, to variable benefits from its involvement with the other entity and has the ability to affect the nature and amount of those benefits through its power over the other entity.
 Thus, an entity controls another entity if and only if the entity has all the following:

- Power over the other entity
- Exposure, or rights, to variable benefits from its involvement with the other entity
- The ability to use its power over the other entity to affect the nature or amount of the benefits from its involvement with the other entity

(IPSAS 35 Paras 19 and 20)

The main elements of the definition of control are further explained Table 5 below (based on IPSAS 35 Paras 23 - 37).

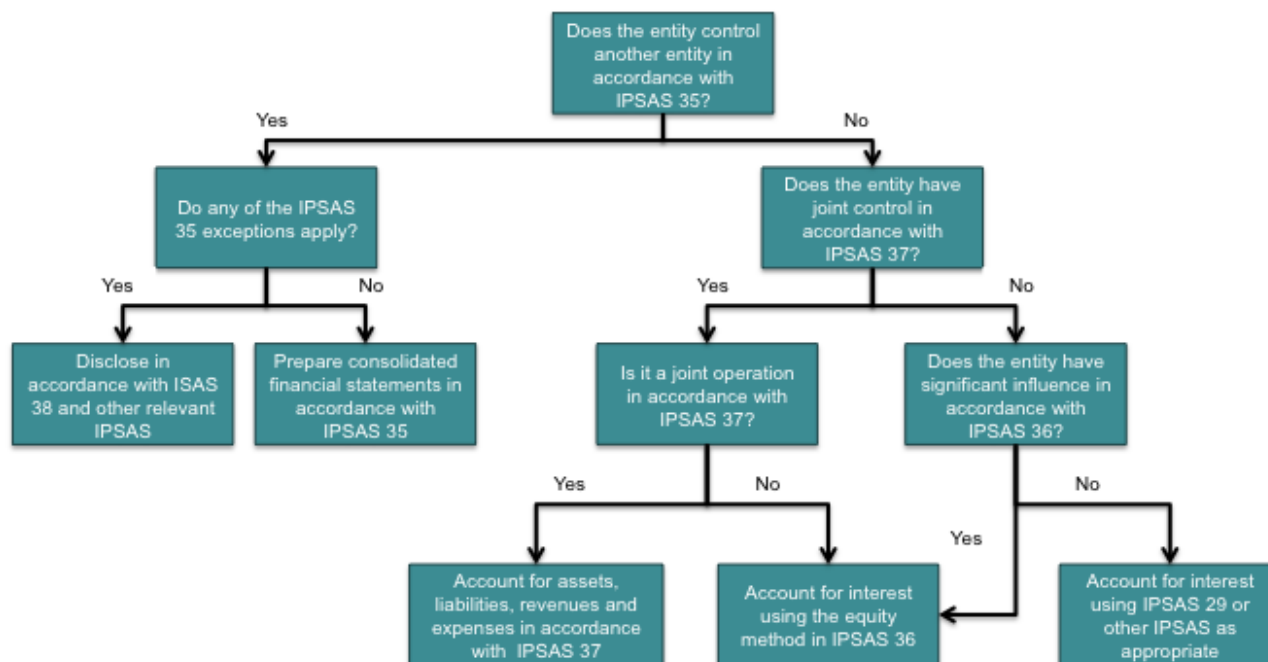
Table 5: IPSAS control criteria

Requirement	Explanation
Power	An entity has power over another entity when the entity has existing rights that give it the current ability to direct the relevant activities. Voting rights, legislative or administrative arrangements, may indicate power. However, regulatory control does not in itself indicate power over the other entity
Benefits	Benefits may be financial or non-financial. Financial benefits include returns on investment such as dividends or similar distributions and are sometimes referred to as "returns". Non-financial benefits include advantages arising from scarce resources that are not measured in financial terms and economic benefits received directly by service recipients of the entity.

Link between power and benefits	An entity controls another entity if the entity not only has power over the entity being assessed for control and exposure or rights to variable benefits from its involvement with the other entity, but also has the ability to use its power to affect the nature or amount of the benefits from its involvement with the entity being assessed for control
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The complication with IPSAS is determining which IPSAS to apply. Figure 6 below provides a summary of the applicable of the different IPSAS and consolidation or other requirements (based on IPSAS 35 IG1).

Figure 6: Determining control for the purpose of preparing financial statements (IPSAS 35)



Section 3.2 above explains the consolidation and other requirements under each of the above standards. Reference should be made to the relevant IPSAS for detailed requirements.

4.4 A comparison of the GFS and IPSAS approach to the consolidation entity

Both IPSAS and GFS use the concept of control to determine which entities should be consolidated. The definition of control is different but in most cases it will result in the same entities being included within the public sector. However, there are three major differences between the IPSAS and GFS approaches as summarised in Table 6 below.

Table 6: Differences between IPSAS and GFS definition of the consolidation entity

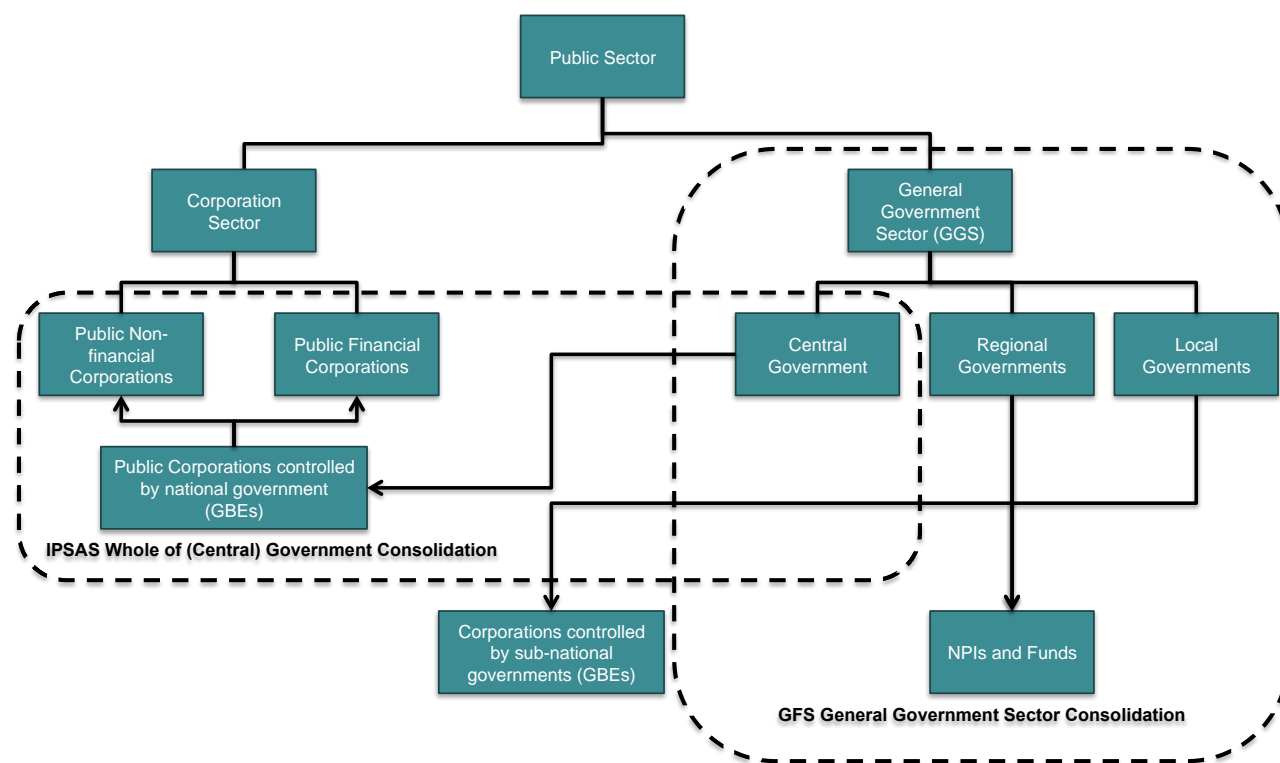
GFS approach	IPSAS approach
<p><i>The statistical reporting unit is an institutional unit, defined as an entity that is capable, in its own right, of owning assets, incurring liabilities, and engaging in economic activities in its own name. The reporting entity may be an institutional unit, but the primary focus is on a group of institutional units (consolidated sector or sub-sector). Control and the nature of economic activities determine consolidation and the scope of the reporting entity. The general government sector does not include institutional units primarily engaged in market activities. (GFS 2014 Box A6.1)</i></p>	<p><i>The reporting unit for financial statements is an economic entity, defined as a group of entities that includes one or more controlled entities. Control is the main criterion that determines consolidation. The whole of government reporting entity, at the highest level of consolidation, may include, in addition to government departments, subnational bodies such as state governments, and government owned businesses that primarily engage in market activities (GFS 2014 Box A6.1)</i></p>
Specific differences	
1. Entity must be resident within territory	No residency requirement
2. Entities are consolidated by sector even if not under common control	All controlled entities are consolidated. Sectors are not relevant.
3. Sectors determine the consolidation structure	Sectors are not identified in an IPSAS consolidation
4. Entities are included within the sector if controlled	Entities are partially included in consolidated financial statements even if there is less than full control (e.g. associates and joint ventures)

The result of these differences is that:

1. Different entities may be included in an IPSAS and GFS defined entity, and
2. Different groups of entities will be consolidated together under IPSAS and GFS.

The diagram in Figure 7 below provides simplified illustration of the differences between GFS and IPSAS consolidation.

Figure 7: Difference between GFS and IPSAS consolidation entity



Notes:

1. The above diagram assumes sub-national governments are not controlled by central government.
2. If sub-national entities are not controlled by central government, then according to IPSAS consolidated financial statements should be prepared for each sub-national government including all entities controlled by that sub-national government
3. The diagram assumes there are no controlled non-resident entities within the public sector. Such entities would be excluded for GFS consolidation but included for IPSAS consolidation

Example 6: Differences between IPSAS and GFS consolidation (1)

Suppose that the Government Air (see earlier examples) is a public corporation and has a wholly owned subsidiary airline based and operating in another country.

1. According to GFS the subsidiary would be non-resident in Country X and therefore not consolidated as part of the public sector of Country X
2. According to GFS the subsidiary is controlled by Government Air, so it is sub-consolidated as part of Government Air and then further consolidated as part of an entity controlled by the Government of X.

Example 7: Differences between IPSAS and GFS (2)

In Figure 5 above the consolidation would be as follows:

- Under GFS the Central Government of X, Province A and Province B, together with NPIs the three governments control, would be consolidated together as the GGS of Country X.
- Under IPSAS there would be three separate consolidation entities:
 - Government X and all entities controlled by that government
 - Province A and entities controlled by that provincial government
 - Province B and all entities controlled by that provincial government.

IPSAS 22 - Disclosure of Financial Information about the General Government Sector

However, it should be noted that IPSAS 22 “Disclosure of Financial Information about the General Government Sector” allows as an additional consolidation statement within the financial statements. This additional statement is the consolidation of the GGS as defined in GFSM (i.e. as in GFS). This is an additional permitted (not mandatory) statement. The IPSAS 22 GGS consolidated statements add to but do not replace the mandatory consolidation statements under IPSAS 35.

4.5 Practical issues in defining the consolidation entity

The analysis so far in this section has been based on the international standards. However, a methodology is required for the practical application of these principles and requirements within each country. Both GFSM and IPSAS adopt a “principle based” approach. Individual countries require “rule based” approach.

Furthermore, within the PEMPAL region there is a requirement for the rules to be legally based. Therefore the definitions of both the entity and the consolidation structure must be defined in accordance with Box 9 below.

Box 9: Rule based approach to defining consolidation entity and structure

Rules for consolidation within individual countries must meet the following conditions:

- **Precise and unambiguous rules for incorporating and classifying entities**
- **Suitable for conversion into legally enforced requirements**
- **Reflect the legal and institutional structure of each country**
- **Accord with the principles set out in GFSM and IPSAS**

From the above requirements it follows that consolidation rules must be developed individually for each country. However, it is possible to set out general guidelines as indicated below.

Institutional units

For most countries institutional units (entities) to be consolidated will be legal entities. However, central and regional governments will each typically be a single legal entity and will require sub-division into individual units for consolidation.

The top-level budget entities (ministries and other main administrators of budget funds) will normally provide a definition already established in the regulatory environment. Hence the rules would define institutional units as:

- Legal entities
- In the case of the government itself top level budget administration authorities

Residency

In general entities controlled by government will be resident within the territory of the government. A very obvious exception would be legal entities registered in another country, e.g. overseas subsidiaries of a public corporation.

If individual countries have more complex issues of residency of entities within the public sector rules would need to be devised for that specific country.

Control

The principles for establishing control are substantially the same for GFS and IPSAS. However, converting such principles into rules is difficult because of the variety of forms of control. The following possible rules are suggested in Table 7 below.

Table 7: Possible rules for defining control

Type of entity	Rules for control
1. Corporate entity that is a market producer	If shares issued - government holds more than 50% of voting rights If shares not issued - government has legal right to appoint Board of Directors
5. Non-Profit Institution (NPI)	Government has legal right to appoint Board of Directors, OR Government has legal right to direct operations of the entity
6. Social Security Fund	Presumed to be controlled by government unless law says otherwise
7. Sub-national levels of government	Controlled by central government unless: <ul style="list-style-type: none"> • Directly elected political leadership with power to direct and control entity, and • Independent authority to raise funds and manage certain functions of government

The above rules will need to be developed and made specific for each country. The rules provide an indication on how the principle based GFS and IPSAS definitions of control can be used to develop a rule-based system.

Sectoral classification

The sectoral classification should already exist if countries are following a GFS budget classification structure. The same structure can then be used for GFS reporting, with the advantage that this enables consistency between budget and reports.

A sectoral classification is not mandatory for IPSAS reporting, but is optional. Furthermore if IPSAS 22 is used to prepare GGS financial statements in addition to the control based statements the sectoral structure will be required.

Compliance with both GFS and IPSAS

The above rule based approach enables compliance with both GFS and IPSAS. However, the actual consolidation groupings may vary between GFS as the former is based on control plus sectors, whereas IPSAS is based entirely on control.

Rule based countries can simplify this further by establishing a legal definition of a reporting entity. This can be used to further define:

1. Which specific government units are reporting entities
2. Whether such entities are part of the GGS or the public corporation sector.

This is the approach adopted in Australia under its new PFMA Act 2013. This law mainly follows the GFS consolidation requirements and definitions for GGS and public corporation sectors.

The next Section on the consolidation architecture indicates how an appropriate architecture will enable reports compliant with either consolidation approach to be generated.

4.6 Approaches to defining the consolidation entity in regional countries

The challenge facing individual governments is to develop and apply a definition of the consolidation entity appropriate to that country's situation.

The above analysis is applied to a number of regional countries to suggest practical approaches to consolidation as indicated in Table 8 below.

Table 8: Analytic structure for regional countries

Country	Definition of the public sector and its sub-sectors at the national level	Analytical division of the public sector into sub-sectors	Notes
Azerbaijan	Definition and composition of the public sector are not set (and are not specified in any law or any other document).	For the purpose of preparing consolidated budget reports by groups of budget entities, and also for the purposes of public finance statistics the approach recommended by the GFSM 2001 is applied.	At present, work is being done on improvement of legal frameworks for the purpose of more detailed coverage of data.
Ukraine	<p>The definition of the general government sector and its sub-sectors is approved by the Order of the State Committee of Statistics of Ukraine of April 18, 2005, "On Approval of the Classification of Institutional Sectors of the Economy of Ukraine".</p> <p>In accordance with approved national accounting standards in the public sector (NASPS), spending units of the public and local budgets, treasury bodies and state special purpose funds were identified as public sector entities, and it is in compliance with the approved classification and GFSM 2001.</p>	<p>For the purpose of preparing consolidated statements according to government finance statistics the approach recommended by the GFSM 2001.</p> <p>For the purpose of preparing statements according to the national system of accounts, the approach recommended by SNA 2008 is applied.</p>	<p>At present, the work is being carried out related to implementation of the NASPs. This will enable consolidated budgetary reports on the public sector as a whole.</p> <p>At present, consolidated financial statements include only two sub-sectors (state and local budgets).</p> <p>The State Special Purpose Funds prepare separate consolidated reports, the data from which is used for preparing consolidated statements on the public sector as a whole.</p>
Russian Federation	There is no set definition of the public (state) sector.	For the purpose of preparing consolidated budget reports by groups of budget entities, and also for the purposes of public finance statistics the approach recommended by the GFSM 2001 is applied.	<p>At present, work is being carried out on formalising definitions of sectors and sub-sectors at the national level, in particular:</p> <ul style="list-style-type: none"> • The budgetary sector; • The general (municipal,) government sector; • The state (municipal) sector.
Republic of Moldova	The definition of the public sector is not specified in the legislative or regulatory frameworks.	For the purpose of preparing consolidated budget reports, and also for the purposes of public finance statistics the approach recommended by the GFSM 2001 is applied.	At present, changes and amendments to the legislation are being considered, which envision a more precise definition of the public sector.

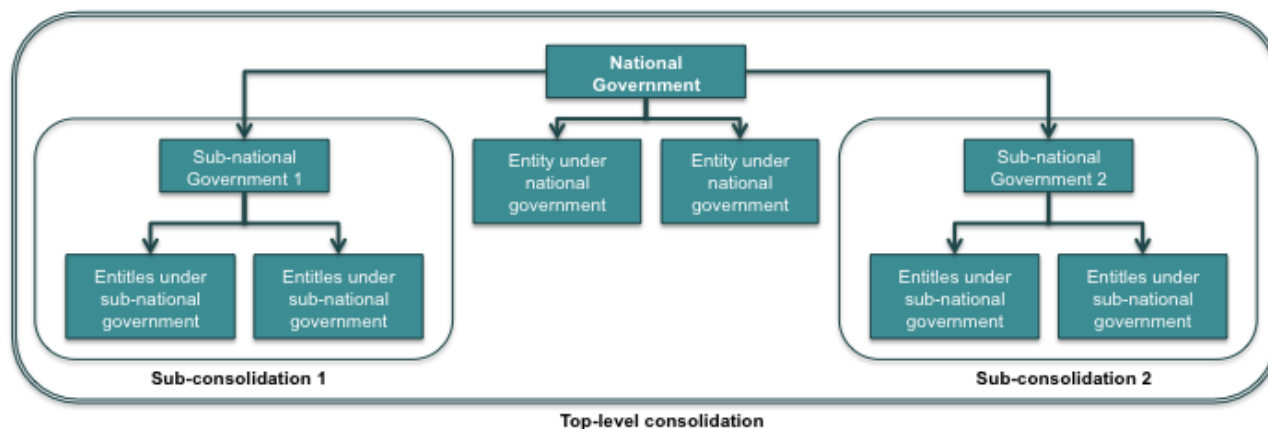
Country	Definition of the public sector and its sub-sectors at the national level	Analytical division of the public sector into sub-sectors	Notes
Georgia	The definition of the public sector is not specified in the legislative or regulatory frameworks.	For consolidated budgetary reports of a group consisting of budgetary entities, and also for reporting on public finance statistics the approach recommended by the GFSM 2001 is applied.	Currently the reform related to expansion of the coverage of the Treasury Single Account is being implemented, so that the TSA would also cover local governments, autonomous formations, and subjects of public law. Therefore, the coverage of the budget compliance reports will increase.
Croatia	The public sector includes the state budget, local and regional units, budgetary and off-budgetary users of the state budget and budgets of local and regional formations.	The general budget includes the central budget (state budget, ministries and their divisions) and off-budgetary units of the state budget and budgets of local and regional formations.	Legal requirement for the State Budget to comply with GFS 2001. However, the public sector also includes public enterprises.

As noted above, consolidation is a way to present information related to a set of entities as if these entities were one whole. Generally, such entities represent all units included in a sector (subsector).

5 The architecture of consolidation

In most countries there will be a hierarchy of consolidation. For example, within the General Government Sector, entities under the control of an individual sub-national government might be consolidated first. These would be sub-consolidations. Then all sub-national governments would be consolidated with the national government. This hierarchical approach is illustrated in Figure 8 below and further discussed in the following subsections.

Figure 8: Hierarchy of Consolidation



This hierarchical approach is useful to enable alternative consolidations for different purposes, e.g. GFS and IPSAS reporting.

5.1 Architecture based on control or sectors

As indicated in previous sections, consolidation may be either on the basis of control or sectors. Figure 9 below illustrates the alternative approaches to consolidation.

Figure 9: Alternative approaches to consolidating government entities

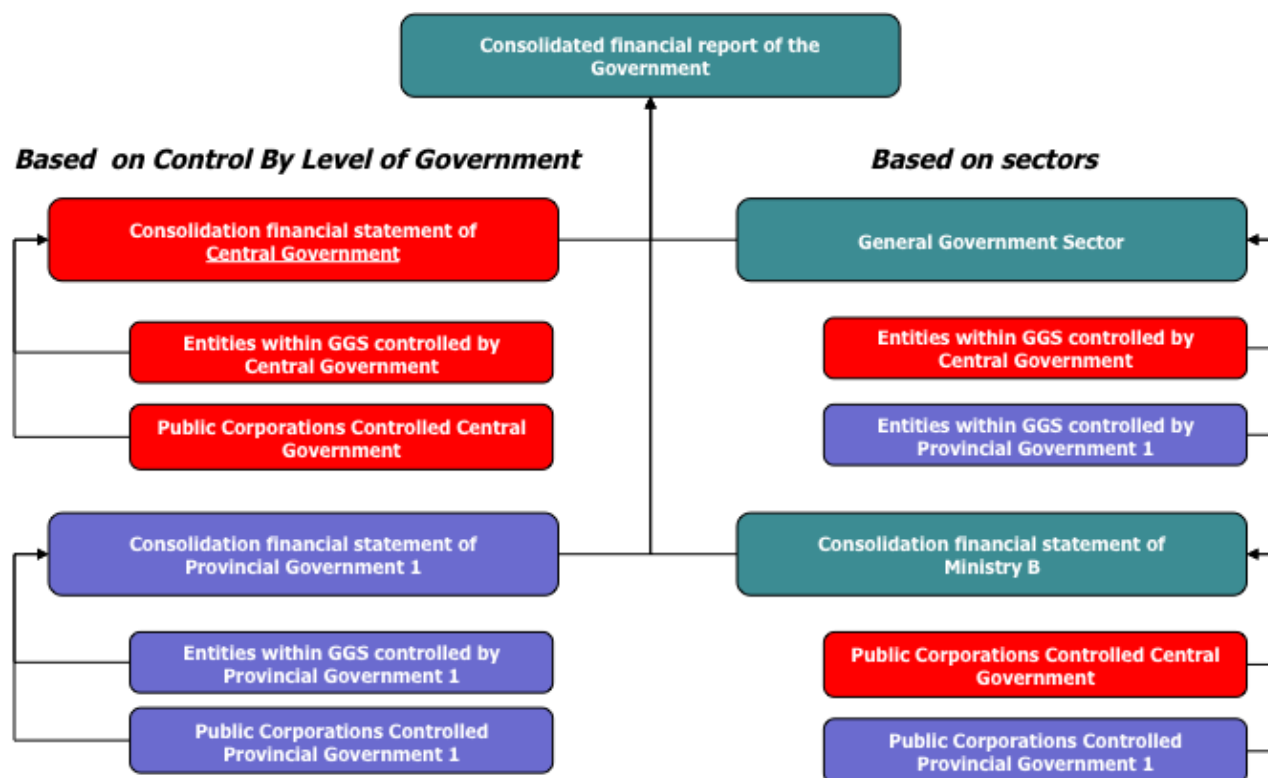


Figure 9 above indicates alternative approaches to consolidation, by sector or by level of government. The two approaches are considered in Table 9 below.

Table 9: Level of government or sector consolidation

Type of consolidation	Appropriateness for GFS	Appropriateness for IPSAS
Level of Government	Not appropriate as does not provide consolidated information on GGS But could be used if a there is sub-consolidation by Sector (as in Figure 9 above) enabling consolidated sectoral information	Appropriate for IPSAS since reflects control structure
Sectoral	Appropriate for GFS since it provides consolidated sectoral information	Not appropriate for IPSAS unless regional authorities are controlled by central government

Therefore it is necessary to consider different approaches to consolidation hierarchies for different purposes. Options of consolidation groupings are further considered in the following sub-sections.

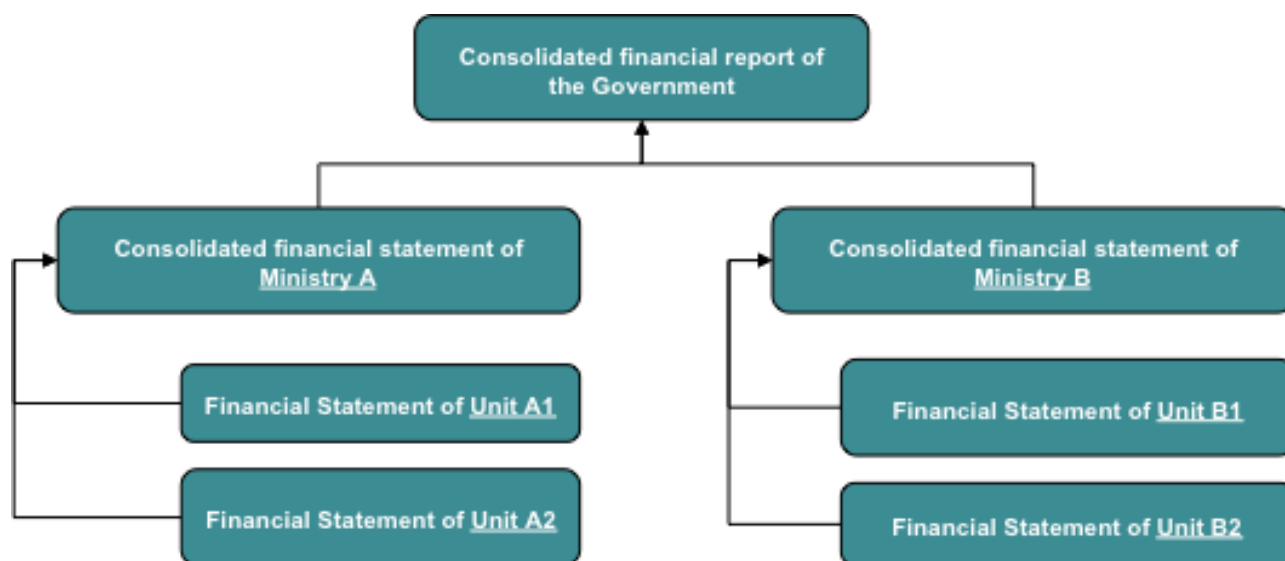
5.2 Centralised or decentralised consolidation

A further practical consideration is whether the consolidation should be hierarchical or centralised. The following models illustrate three options.

Model 1 – hierarchic consolidation architecture

Consolidation follows a “tree” structure with consolidated units being consolidated at the next level up within the hierarchy of government. This is illustrated in Figure 10 below.

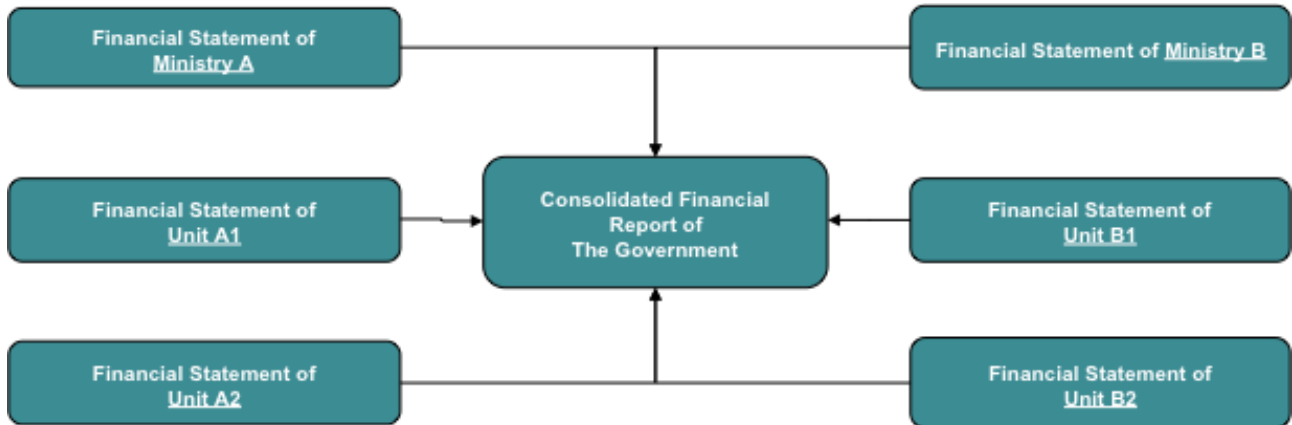
Figure 10: An example of hierarchic consolidation architecture



Model 2 – central consolidation architecture

Under a centralised approach the consolidation of all the entities to be consolidated is performed as one centralised exercise, as illustrated Figure 11 below.

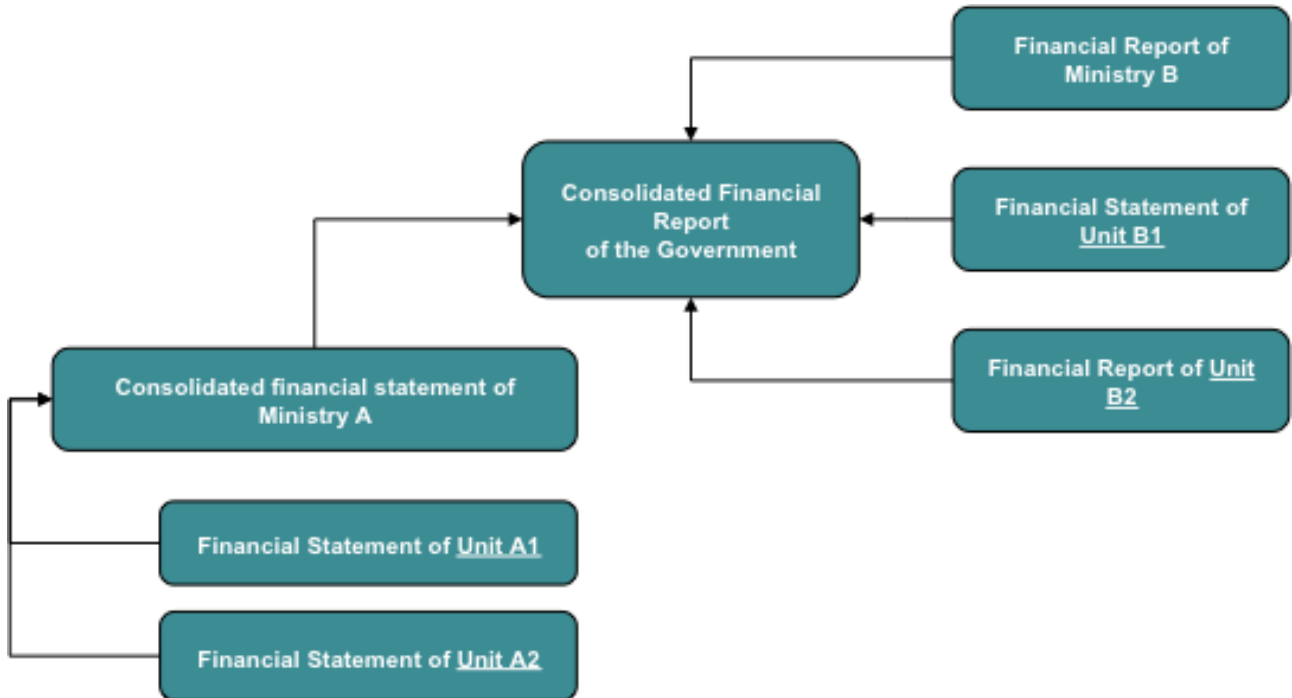
Figure 11: An example of a centralised consolidation architecture



Model 3 – mixed architecture

It is also possible to combine centralised and hierarchic consolidation architecture so that some entities use the hierarchic approaches whilst others are consolidated centrally, as illustrated in Figure 12 below.

Figure 12: An example of mixed architecture of consolidation



An analysis of advantages and disadvantages of the above models is provided in Table 10 below.

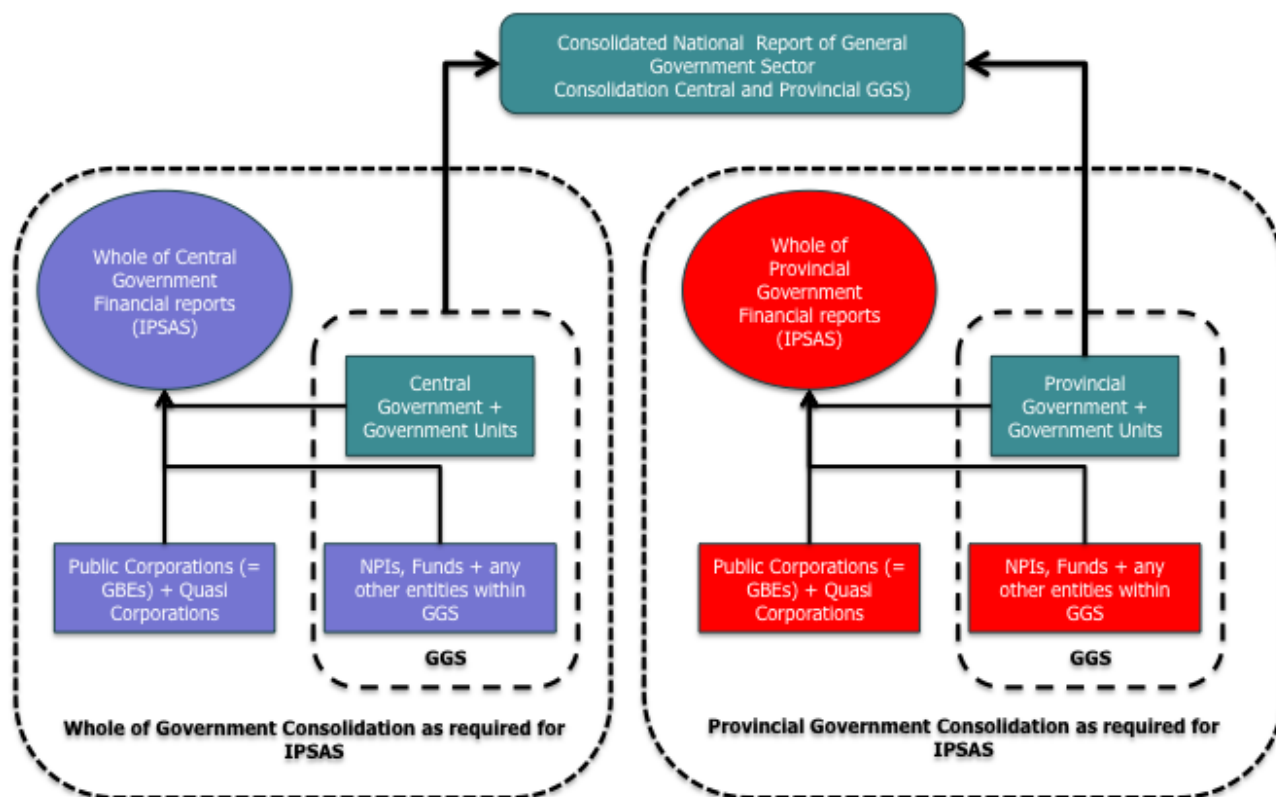
Table 10: Advantages a disadvantages of consolidation hierarchy

Architecture	Advantages	Disadvantages
Hierarchic	More manageable process especially if large number of entities to be consolidated Provides consolidated information at intermediate levels of government	Requires adequately trained staff at multiple levels of government
Central	By concentrating consolidation work reduces requirement for trained staff at intermediate levels of government	Only centralised consolidated information is available May be complex to manage if many entities to consolidate
Mixed	Reduced training requirement as compared to hierarchical Some lower level consolidated information available	More training than centralised Not as much consolidated information as hierarchical

5.3 Designing an architecture to enable GFS and IPSAS consolidation

As indicated above the consolidation architecture can be designed so as to enable consolidation for both GFS and IPSAS reporting. The diagram in Figure 13 and the text below explains the approach.

Figure 13: Consolidation architecture to enable GFS and IPSAS reporting



Notes:

1. This example assumes there is central government plus one provincial government (the latter not controlled by central government)
2. This example also assumes there are no controlled non-resident entities. If such existed within the GGS they would have to be consolidated separately so they could be included in IPSAS reporting but excluded for GFS reporting.
3. The provincial consolidation group would be replicated for every sub-national group not controlled by central government if there is more than one.

Using the architecture described in Figure 13 above it is possible to use a single consolidation exercise to generate:

1. A consolidation as required by IPSAS for each controlled group of entities, e.g. national and provincial governments
2. Consolidated reporting on the GGS for all entities within a particular country thus enabling GGS and IPSAS 22 reporting.

Thus appropriate design of the consolidation architecture enables compliance with different reporting requirements and entity definitions.

5.4 A practical approach to consolidation architecture

The concepts of the consolidation architecture in this section can be used to design a consolidation architecture for each country that enables the consolidation requirements of both GFS and IPSAS to be met and at the same time comply with the legal and institutional structure of each country.

The principle requirements of such architecture are summarised in Box 10 below.

Box 10: Requirements of a country specific consolidation architecture

1. **Based on the legal and institutional structure of the country**
2. **Contain clear rules that can be incorporated into laws and regulations for implementation by government staff**
3. **Ensure consistency in accounting policies and practices across all entities to be consolidated**
4. **Identify and consolidate at levels of independent control within the hierarchy of governments (local, regional, state) for the purpose of IPSAS financial reports**
5. **At each level identify and consolidate separately GGS and public corporations sector**
6. **Have special procedures to identify and segregate from the consolidation any public sector controlled entities resident in other countries.**
7. **For national GGS reporting consolidate the GGS sectors as consolidated at each of the national and subnational government levels.**

An architecture as described above will be feasible to implement and will enable reporting compliant with both GFS and IPSAS and also with the national requirements for transparency and accountability.

6 Methodology of Consolidation in the Public Sector

6.1 Special features of public sector consolidation

As explained in Section 2.3 above the basic principles of consolidation apply to both the public and private sectors. Practical differences arise from different ownership, legal status, outputs and controls over the public sector and in particular the general government sector:

- **Ownership** - often prescribed by legislation and regulation instead of through ownership of shares
- **Legal status** - often established by legislation specific to each entity
- **Outputs** - social benefits instead of goods or services for sale
- **Controls** - administrative rather than legal and regulatory bodies (in fact some GGS entities may be the regulatory bodies for the commercial sector).

None of the above special features of public sector entities change the principles of consolidation, but they may change the practical application of such principles.

6.2 The methodology of consolidation

This sub-section explains the basic methodology of consolidating using a series of examples. These examples follow the basic principles set out in Box 2 on page 5.

Example 8: Consolidation of wholly owned controlled entity

Within a Country X, the company “Government Air” (already used in previous examples) is a registered company that issues shares. All of the shares are owned by the central Government of Country X and for administrative purposes the Ministry of Transport manages Government Air. Government Air only provides services to Government staff and does not charge market prices - therefore it is an NPI within the GGS. Its only base of operations is within the territory of Country X.

For simplicity it is assumed that the Ministry of Transport defined as an institutional unit within the GGS and that the Ministry of Transport controls no other entities.

The table below summarises the balance sheets and operating statements of the Ministry of Transport and Government Air, the consolidation process and consolidated results.

Description	Ministry of Transport	Government Air	Aggregated (Step 1)	Flows/ balances between entities	Consolidated (Step 2)
Balance Sheet					
Non-financial assets	2,000	1,500	3,500		3,500
Financial assets					
Shares in Government Air	600		600	600	0
Receivable from Ministry of Transport		400	400	400	0
Other	400	200	600		600
Total assets	3,000	2,100	5,100	1,000	4,100
Liabilities					
Other	300	1,500	1,800		1,800
Liability to Government Air	400		400	400	0
Total liabilities	700	1,500	2,200	400	1,800
Net assets	2,300	600	2,900	600	2,300

Description	Ministry of Transport	Government Air	Aggregated (Step 1)	Flows/ balances between entities	Consolidated (Step 2)
Operating Statement					
Revenue					
Other revenue	800		800		800
Grant receivable		400	400	400	-
Total revenue	800	400	1,200	400	800
Expenditure					
Other	300	150	450		450
Grant to Government Air	400		400	400	
Total expenditure	700	150	850	400	450
Operating surplus/deficit	100	250	350	-	350

6.2.1 Minority interests

In some instances a public sector entity may control another entity, but there may be a significant external ownership of the entity. For example a government may own 51% of the shares in a company and private investors the other 49%. In such a case government controls the entity, but there is a 49% minority interest. If the entity concerned is a company, as in the example, then the minority interest can easily be quantified as the percentage of shares held externally. If the controlled entity does not have shares then reference must be made to the laws creating the entity to quantify the minority interest.

The requirement for both GFS and IPSAS is that the minority interest must be identified and excluded from the consolidation: "A controlling entity shall present non-controlling interests in the consolidated statement of financial position within net assets/equity, separately from the net assets/equity of the owners of the controlling entity." (IPSAS 35 Para 47)

Example 9: Consolidation with minority interest

Assume the information as in Example 8 except that a shareholder external to government owns 40% of the shares of Government Air. This minority interest has to be separately identified and deducted from the consolidated information as indicated below.

Description	Ministry of Transport	Government Air	Aggregated (Step 1)	Flows/ balances between entities	Consolidated (Step 2)	Minority interest in Air 40%	Consolidated excluding minority interest
Balance Sheet							
Non-financial assets	2,000	1,500	3,500		3,500	600	2,900
Financial assets							
Shares in Government Air	600		600	600	0	0	0
Receivable from Ministry of Transport		400	400	400	0	160	-160
Other	400	200	600		600	80	520
Total assets	3,000	2,100	5,100	1,000	4,100	840	3,260
Liabilities							
Other	300	1,500	1,800		1,800	600	1,200
Liability to Government Air	400		400	400	0		
Total liabilities	700	1,500	2,200	400	1,800	600	1,200
Net assets	2,300	600	2,900	600	2,300	240	2,060

Description	Ministry of Transport	Government Air	Aggregated (Step 1)	Flows/ balances between entities	Consolidated (Step 2)	Minority interest in Air 40%	Consolidated excluding minority interest
Operating Statement							
Revenue							
Other revenue	800		800		800	-	800
Grant receivable		400	400	400	-	160	160
Total revenue	800	400	1,200	400	800	160	640
Expenditure							
Other	300	150	450		450	60	390
Grant to Government Air	400		400	400		-	-
Total expenditure	700	150	850	400	450	60	390
Operating surplus/deficit	100	250	350	-	350	100	250

Though not indicated the consolidation process for cash flow statements will be carried out using the same approach as indicated in the examples.

6.2.2 Budget consolidation

The same principles and methodology apply to the preparation of a budget and the comparison of the budget with actual expenditures and revenues.

In the preparation of the budget for a public sector entity that includes controlled entities, flows between entities should be eliminated. This means that the taxes payable by one Ministry to central tax authority should not be recorded as expenditure of the paying Ministry or receipts of the tax authority.

There are two exceptions to this rule:

1. Employer social contributions, whether paid to social security or government pension funds, are treated as being payable to the employee; and
2. Taxes withheld by government units from the compensation of their employees, such as pay-as-you-earn taxes, should be treated as being paid directly by the employees.

According to IPSAS where an entity prepares a budget for itself and controlled entities (e.g. the National Budget for the public sector) the financial statements must include a comparison of the original budget, the revised budget and the actual outcomes (IPSAS 24). If the original budget is a consolidated budget (as will normally be the case for national budgets) then the comparison under IPSAS 24 must also be consolidated.

However, most countries do not publish a budget with the same coverage as that required under either IPSAS or GFS, for example:

- National budgets do not normally include consolidated public corporation information
- National budgets may show flows to or from other entities within the GGS as transfers (e.g. grants) because these entities are not controlled by central government.

If there is no published budget with the same coverage as the IPSAS financial reports, then there is no IPSAS requirement for a budget comparison.

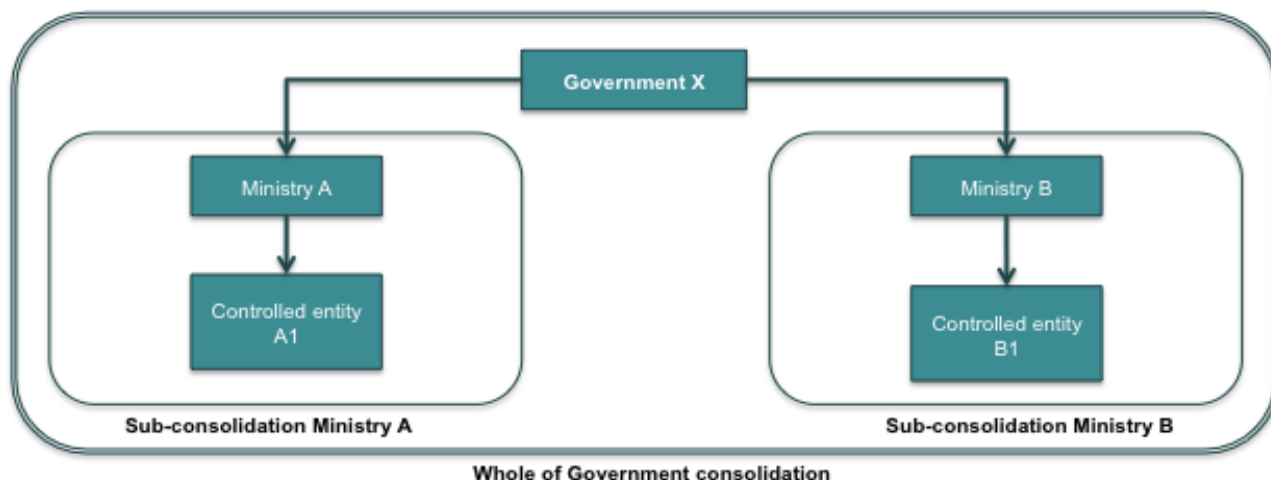
6.3 Elimination of inter-entity flows and balances

A key element of consolidation is the elimination of flows and balances between individual entities within the consolidation. The principle is illustrated in the above examples. In practice identifying and recording such flows and balances can be a major challenge.

A further problem is that within a hierarchical consolidation, what are external flows at a lower level of consolidation may become internal flows at a higher level of consolidation.

Example 10: Inter entity flows

Government X consists of two Ministries: A and B. Ministry A controls one entity A1; Ministry B also controls one entity B1. The only transaction between any of the entities is that A1 lends B1 €10,000. Consolidation is at two levels: the Ministries individually and then the whole of government as illustrated below.



The financial information and the three consolidations are summarised in the table below.

Description	Ministry A	Entity A1	Consolidated Ministry A	Ministry B	Entity B1	Consolidated Ministry B	Whole of Government Consolidation
Assets							
Loan from A1 to B1	\$ -	\$ 10,000	\$ 10,000	\$ -		\$ -	
Other	\$ 20,000	\$ 5,000	\$ 25,000	\$ 30,000	\$ 14,000	\$ 44,000	\$ 69,000
Total	\$ 20,000	\$ 15,000	\$ 35,000	\$ 30,000	\$ 14,000	\$ 44,000	\$ 69,000
Liabilities							
Loan from A1 to B1	\$ -	\$ -	\$ -		\$ 10,000	\$ 10,000	
Other	\$ 7,000	\$ 4,000	\$ 11,000	\$ 17,000	\$ 3,000	\$ 20,000	\$ 31,000
Total	\$ 7,000	\$ 4,000	\$ 11,000	\$ 17,000	\$ 13,000	\$ 30,000	\$ 31,000
Net equity	\$ 13,000	\$ 11,000	\$ 24,000	\$ 13,000	\$ 1,000	\$ 14,000	\$ 38,000

Explanation

At the level of consolidation of Ministry A balance lent by Unit A1 to Unit B1 is an external balance and will not be eliminated on consolidation (shaded in above example). However, at the level of consolidation of the whole of government X such a balance is an internal balance and must be eliminated on consolidation.

Comment

The above example illustrates a specific problem with a hierarchical consolidation - external flows and balances at a lower level of consolidation may become internal flows and need to be eliminated at higher levels of consolidation.

6.3.1 Major flows to be eliminated on consolidation

Most flows between entities within the consolidation will be of a limited number of categories and easily identified as summarised below in Table 11 below.

Table 11: Major categories of flows and balances to be eliminated on consolidation

Category	Description	When eliminated
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Category	Description	When eliminated
1. Taxes and fees	Payable by state owned entities to taxing or fee charging authority	Any consolidation that includes payer and payee
2. Dividends and share of profits	Payable usually by market producers (corporations or quasi corporations) to controlling Ministry or other government body	Consolidation of controlling entity (IPSAS) or whole of public sector (GFS)
3. Interest payments and receipts	Interest on loans from one entity to another entity when both are within the public sector	If lender and borrower are both within the consolidation
4. Grants and subsidies	Made from one public sector entity to another	Consolidation of controlling entity (IPSAS or GFS) or within a sector (GFS)
5. Payments for goods or services	Either resulting from a transfer or a payment to market producer (public corporation or quasi corporation)	Most difficult to identify and see notes on materiality below. Should be eliminated whenever both supplier and purchaser are consolidated together
6. Shareholdings and other equity investments	Where a controlling entity within the public sector owns shares or equity investments in an entity that it controls	Commonly applies to GBEs that issue shares or similar equity instruments. Eliminated when consolidated as controlled entities (IPSAS) or as part of the public sector (GFS)
7. Loans and borrowings	When one public sector entity lends to another. Can occur when loans to a government are on-lent to public sector entity	Whenever both lender and borrower are included in the same consolidation entity
8. Receivables and payables	Can arise from a variety of situations including payments for goods and services	As with payments for goods and services if small and irregular may be difficult to identify. Should be eliminated whenever both entities are consolidated together

The above list is not comprehensive but does indicate the major categories of flows and balances to be eliminated on consolidation.

6.3.2 *Establishing procedures for automatically identifying intra-entity flows*

In a simple consolidation with few entities it is possible to individually identify and eliminate intra-entity flows and balances. But with a larger consolidation with many entities involved such an ad hoc approach is not feasible.

In a computerised accounting system there are three possible approaches to identifying such flows and balances:

1. Design the chart of accounts so that there is specific code to identify intra entity flows and balances
2. Design of the IT systems so that intra-entity transactions and balances can be flagged and identified

3. Tools within individual software packages to facilitate consolidation - these will depend on the functionality of each application.
4. If the payee and recipient are defined using unique identifiers, this will provide the necessary structure for this.
For example, if government reporting entities have a unique vendor identifier (ID) from the Chart of Accounts (the institutional number) then these IDs It is quite common that the amounts reported by one entity as owing to one entity can be highlighted in the accounting system for elimination. The same could apply for receipts - the payee could also have a unique number (the same government institution number) and this will highlight what may need to be eliminated.

The approach adopted will form part of the consolidation planning process and will require consultation with IT staff and/or the suppliers of IT applications used by the government.

Materiality and intra-entity flow

As indicated above identifying all of the intra entity flows and balances may be difficult.

Example 11: Example of low value intra-entity transactions

A Government survey office may sell maps to the general public for a nominal cost. If another Ministry was to occasionally buy maps this would be a transaction between entities in the public sector and should be eliminated when the two entities are consolidated together. However, the amounts involved will be small and the transactions too infrequent to establish formal recording systems.

The GFS states “*practicality should be kept in mind: the re- sources devoted to consolidation and the level of detail applied in consolidation should be in direct proportion to their fiscal significance.*” (GFSM 2014 Para 3.165).

IPSAS has no such specific statement, but the general principle of materiality applies: “*Information is material if its omission or misstatement could influence the discharge of accountability by the entity, or the decisions that users make on the basis of the entity’s [Financial Statements] prepared for that reporting period.*” (IPSAS Conceptual Framework Para.3.32)

Therefore for both GFS and IPSAS reporting it is not necessary or desirable to identify every intra-entity flow or balance. Only those that are material as defined above need be identified.

Accountants and treasury staff with a background in countries with a legalistic approach to accounting may find the use of approximations based on general guidance difficult. There is a desire for even such approximations to be specified in law. But the whole point of the approach described is to apply general principle in deciding what items to include.

Amounts of balances and flows differ between reporting entities

It is quite common that the amounts reported by one entity as owing to another entity differ from the amounts the other entity believes is owed. Differences arise because of recording and classifying errors. The GFS approach is as follows: *“Resolving these discrepancies [between reporting entities] will promote proper consolidation and improve the overall quality of GFS compiled. However, where a discrepancy cannot be resolved, decisions need to be made about which unit or group of units has the most reliable source data.”* (GFSM 2014 Para 3.165)

Non-monetary flows and balances

Sometimes the transactions between entities will not be monetary, for example the transfer of non-financial assets. In such cases the rules of valuation developed in GFS and IPSAS will be applied.

6.4 Sequencing the implementation of consolidation

It is useful for countries to consider sequencing issues when implementing consolidated reporting. The following provides a generalised sequence of actions in the consolidation process. If a country has not as yet published consolidated financial statements that include all of the entities in appropriate structures as described in the preceding sections of this Guidance Note it is necessary to develop a plan for such consolidated reporting. The following provides a generalised sequence of actions in the consolidation process.

Table 12 below converts this generalised approach into an action sequence.

Table 12: Plan for including all required entities in consolidation

Stage	Description
1. Develop rules for application of consolidation requirements	As described in Section 4.5 develop a country specific set of rules for identifying and classifying entities to be consolidated
2. Identify and classify entities to be consolidated	Apply the rules developed above to prepare a comprehensive list of all entities to be consolidated
3. Plan consolidation architecture and reporting structure	This is explained in Section 5 below
4. Identify actions required to be able to consolidate each group of entities	Actions will include addressing issues such as year ends, accounting policies, information requirements, audit requirements, identifying inter entity transactions, etc
5. Plan phased sequence for incorporating entities not already included in consolidation	Phasing may be by a combination of level of government, sector and controlling entity as appropriate for each country. Time allowed for each phase should be realistic

Stage	Description
6. Plan required training and technology for implementing consolidation plan	Training will be required for additional staff that will be required: <ul style="list-style-type: none">• Staff in entities to be consolidated on information requirements• Auditors on audit reports• Staff to carry out consolidation It is also possible that additional software will be required, modules added to an existing IT systems, or modifications made to existing systems.
7. Implement plan	Implement the phased consolidation plan as a major project with appropriate project management, milestones and monitoring

The detail of the plan will have to be developed for each country, but the above list provides an indication of the necessary steps.

7 Exceptions from consolidation

7.1 Reasons for exceptions from consolidation

Entities may not be consolidated for one of four groups of reasons:

1. Specific exemptions from the consolidation requirements under GFS or IPSAS
2. The law precludes consolidation even though it is required by GFS and/or IPSAS
3. Entities are not consolidated even though required because it is not practicable or economic to consolidate the entities.
4. Consolidation not appropriate e.g. for statistical reporting

These reasons are explained below.

7.2 Specific exceptions allowed under GFS and IPSAS

The general principle of both GFS and IPSAS is that all entities controlled by a public sector entity are consolidated. However, there are specific exemptions under both sets of requirements.

7.2.1 *Exceptions to consolidation under GFSM 2014*

Although GFSM 2014 has no list of exemptions, in fact there are a number of exceptions as summarised below.

Table 13: GFSM 2014 exemptions to consolidation requirements

Exemption	Explanation
1. Entities resident outside the territory	Only entities resident in the territory of the country are included in GFS consolidation
2. Fiscal activities of Special Purpose Entities	These are entities registered within the country but all of their operations are conducted outside the country. Though consolidated, their fiscal activities are excluded.
3. Entities that do meet the requirements to be defined as an institutional unit	Some institutional entities do not meet the requirement to be classified as institutional units, for example some joint operations, provident funds, etc. Even though the entity may not be consolidated the fiscal activities should be consolidated if controlled by government
4. Sovereign Wealth Funds incorporated outside the country	These are a special case and are treated as a separate institutional unit in the financial corporations sector
5. Any entities that do not fall within the definition of the public sector	The overriding requirement is that the entity must be part of the public sector. Furthermore for consolidation as part of the GGS it must fall within the definition of the GGS.

The GFS sector approach will inevitably lead to many issues as to the delineation of institutional units and then allocating those units to specific sectors for consolidation.

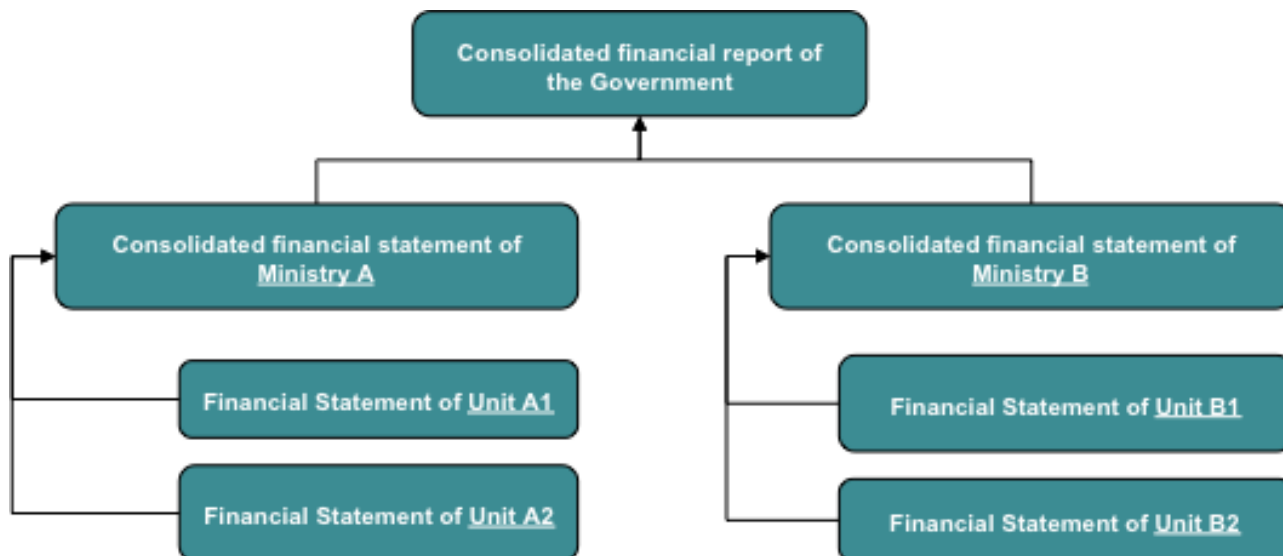
7.2.2 Exceptions under IPSAS

IPSAS 35 requires any entity that prepares financial statements and controls another entity to present consolidated financial statements. The only two exceptions under IPSAS 35 are summarised below¹.

1. An intermediate controlling entity within a hierarchy of consolidation

This situation is illustrated in Figure 14 below.

Figure 14: Intermediate consolidation entity exempted from consolidation requirement



In the above example Ministries A and B are not required to publish consolidated financial statements provided:

- The information needs of users are met by its controlling entity's consolidated financial statements, and, in the case of a partially owned controlled entity, all its other owners, including those not otherwise entitled to vote, have been informed about, and do not object to, the entity not presenting consolidated financial statements, and
- Its debt or equity instruments are not traded in a public market, and
- It did not file, nor is it in the process of filing, its financial statements with a securities commission or other regulatory organization for the purpose of issuing any class of instruments in a public market, and
- Its ultimate or any intermediate controlling entity produces financial statements that are available for public use and comply with International Public Sector Accounting Standards

¹ Note that the exemption for temporary control is no longer available under IPSAS 35.

(IPSASs), in which controlled entities are consolidated or are measured at fair value through surplus or deficit in accordance with this Standard.

Note that all four conditions must be met to obtain the exemption (IPSAS 35 Para 5).

2. Investment entities

A controlling entity that is an investment entity shall not present consolidated financial statements if it is required, in accordance with paragraph 56 of [IPSAS 35], to measure all of its controlled entities at fair value through surplus or deficit. (IPSAS 35 Para 7)

An investment entity is an entity that:

- (a) Obtains funds from one or more investors for the purpose of providing those investor(s) with investment management services;
- (b) Has the purpose of investing funds solely for returns from capital appreciation, investment revenue, or both; and
- (c) Measures and evaluates the performance of substantially all of its investments on a fair value basis. (IPSAS 35 Para 14)

The only investment entities controlled by government in the regions are likely to be sovereign investment funds. Note that the investment entity must itself be consolidated in the financial statements of its controlling entity.

7.3 Consolidation precluded by law

A country may create a specific law, or regulation under the law, which forbids the consolidation of certain entities. Such a law or regulation is specific to the country concerned.

It is obligatory for the financial statements to accord with the law of the country. However, in so doing it may not be possible to fully report in accordance with GFSM 2014 or with IPSAS.

- In the case of GFS the GFS reports may be made using best estimates for any missing data
- In the case of IPSAS it is necessary to report in the Notes to the financial statements the fact and nature of any non-compliance with IPSAS. However, the fact that non-compliance is reported does not make the financial statements compliant - it merely mitigates the effect of non-compliance

7.4 Exception because consolidation is not practical

There are a number of possible reasons why consolidation may not be possible:

- During a phased implementation of the consolidation requirement the stage may not have been reached where a particular entity is to be consolidated
- Information on the entity is not available because of war or civil conflict

- The costs of obtaining the information outweigh the potential benefits from inclusion of an entity in the consolidation.
- Other problems of obtaining the information required for consolidation.

In all of the above cases the fact of non-consolidation should be reported in the notes together with an explanation.

7.5 Consolidation not appropriate

As indicated in Section 3.4 on page 21 consolidation is not appropriate for national income reporting (UN SNA 2008 and ESA 2010).

Consolidation is also not appropriate whether information is required on specific entities, e.g. individual NPIs or public corporations. In some cases it may be necessary to review both consolidated and unconsolidated information.

8 Reporting Consolidated information

8.1 Overview of consolidated reporting

8.1.1 Requirements and need for publication of consolidated information

Section 2.2 of this report indicated that the objective of consolidation is to provide a comprehensive financial picture of a group of entities as though they were a single entity. Section 2.5 further indicated that the end products of consolidation are reports.

The different categories of reports were summarised as follows:

1. Consolidated budget documents
2. Consolidated financial reports for external users:
 - a. Audited financial statements
 - b. Statistical reports required by external users - GFS 2014 reports and also for members of the European Union reports in compliance with ESA 2008.
 - c. Interim and special reports, e.g. budget execution
3. Consolidated financial reports for management (not published)

This section examines in more detail the format and requirements for reports.

8.1.2 Reporting objectives

Reports are a tool of communication and as such have a range of uses by different stakeholders in the public sector. Some of the most important objectives of consolidated reporting include the following:

- **Resource management** - to enable political leaders to use fiscal resources to achieve policy goals
- **Fiscal transparency** - as set out in the IMF Code of Fiscal Transparency (2014 update) and the OECD Best Practices in Fiscal Transparency (2002) to make the public sector transparent to citizens and other stakeholders
- **Accountability** - to make public sector organisations and individuals accountable to citizens
- **Management** - to enable managers and staff in the public sector to better perform their functions
- **Monitoring and control** - providing a monitoring tool to enable effective control over processes and people.

The matrix in Table 14 links the different types of consolidated reports to the reporting goals.

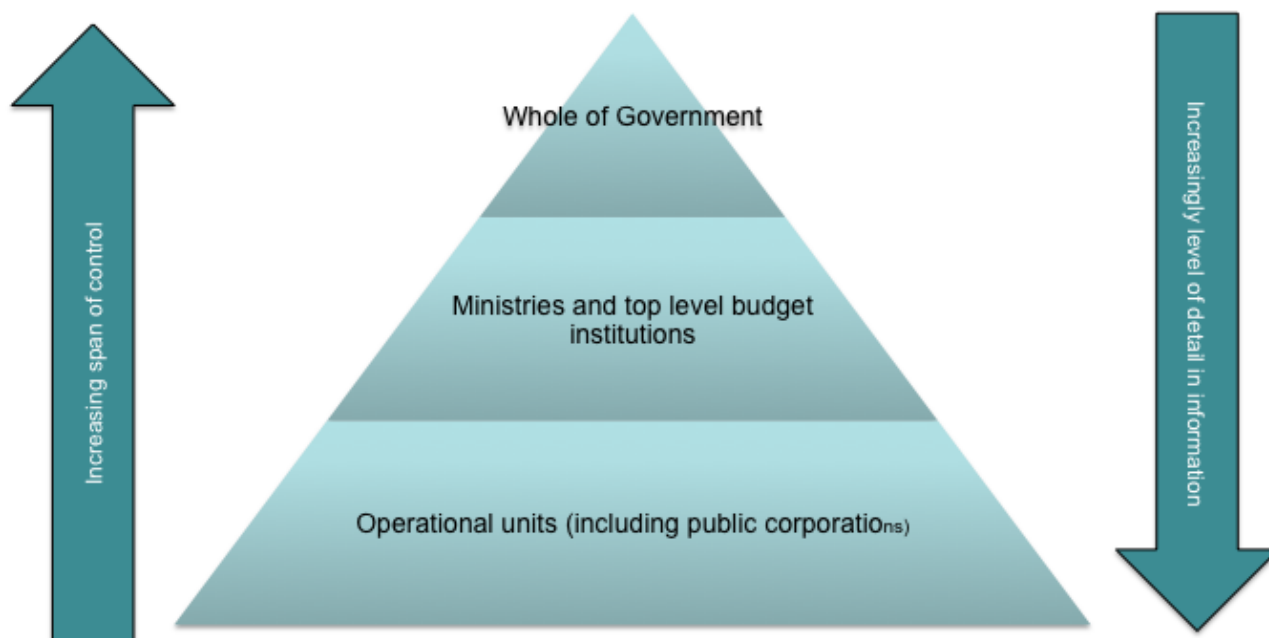
Table 14: Matrix linking consolidated reports and goals

Consolidated Report	Resource management	Fiscal Transparency	Accountability	Management	Monitoring & control
Budget	☐	☐	☐	☐	☐
Financial Statements		☐	☐		☐
Statistical reports		☐			
Interim reports		☐	☐		☐
Management reports	☐			☐	☐

The following sections consider the major categories of reports and the relevant standards and requirements.

8.1.3 Management and reporting hierarchy

There is a hierarchy of reporting linked to the hierarchy of management control as illustrated in Figure 15 below.

Figure 15: Hierarchy of management and reporting

As the level of government moves upwards from operational units to the whole of government the span of control increases but the requirement for detail decreases. The reporting structure and content must reflect the level of government or review for which the reports are intended.

8.1.4 Whole of government financial reporting

Whole of government financial reports are a recent development. Until recently reporting at the whole of government level has only consisted of budget execution and statistical reporting. A number of factors have contributed to the development and publication of comprehensive whole of government financial reporting embracing the whole of the public sector. At the present time only a limited number of countries have published comprehensive whole of government financial reports.

The concept of whole of government financial reporting is both laudable and challenging. Such high level consolidated financial reports provide citizens and outside parties with comprehensive information on the fiscal activities of governments. The value of such whole of government reporting is further enhanced when the financial reports comply with international standards (i.e. IPSAS) and are independently audited by a Supreme Audit Authority (SAI).

However, whole of government financial reporting presents major challenges. These challenges are typically of several types:

- **Technical** - consolidating information from different entities using different accounting systems
- **Information** - obtaining all of the required information within the prescribed time limits
- **Standardisation** - because the implementation of classification structures and accounting policies across the whole of the public sector presents major issues.

In the UK it took a team of qualified experts 10 years to be able to publish whole of government financial reports. The resulting document extends to some 227 pages (UK Whole of Government Financial Statement 2013-14: www.gov.uk).

So far most countries that have published whole of government financial reports have used national standards rather than IPSAS, e.g. the UK, Australia, New Zealand. This does indicate the challenge facing regional countries attempting to prepare IPSAS compliant whole of government financial reports.

However, IPSAS compliant whole of government financial reports would not include sub-national entities that are not controlled by central government.

8.2 Consolidated budget reports

Most regional countries are moving towards, or have adopted, GFS classification for budget documents.

At aggregated level budgets should be consolidated using the principles explained in this Guidance Note. Such consolidation will be necessary to enable comparability with consolidated financial reports. However, for some purposes it will be necessary to identify flows between budget entities. Examples include:

- Tax payments by government agencies - such agencies will need to identify and budget for such payments

- Dividend payments and share of profits from public corporations and quasi corporations - the extent of such contributions to the overall resources of the government is important information.

These examples emphasise the need for a budget hierarchy as described in Figure 15 above, and also the issue of intra entity flows at different levels of the consolidation hierarchy in Figure 14. Information and intra entity flows becomes increasing high level with detail lost as the budget moves to a higher level.

A requirement of IPSAS 24 is for a comparison of actual outturns and the budget. It is further required that that *“All comparisons of budget and actual amounts shall be presented on a comparable basis to the budget”* (w Para 31). This means that the financial information should be consolidated in the same format as the budget statements.

However, as explained in Section 6.2.2 on page 49 most countries do not publish a budget with the same coverage as that required under either IPSAS or GFS, for example:

- National budgets do not normally include consolidated public corporation information
- National budgets may show flows to or from other entities within the GGS as transfers (e.g. grants) because these entities are not controlled by central government.

As explained in Section 6.2.2 if there is no published budget there is no requirement for a budget comparison. For this reason the very few countries that have so far published IPSAS compliant whole of government financial

8.3 Consolidated GFS reports

As indicated in this Guidance Note GFS statistical reports must be consolidated in the format prescribed in GFSM 2014. The GFS formats are issued annually by the IMF in the form of a pack of Excel spreadsheets to be completed by each country.

Box 11: GFS Reporting Tables 2014

1. Statement of Operations (not directly comparable to the IPSAS Statement of Financial Performance as non-transactional flows are excluded from the GFS statement)
2. Statement of Sources and Use of Cash (equivalent to IPSAS Cash Flow Statement)
3. Statement of Flows and Stock Position (no direct IPSAS equivalent this breaks down the change in value of each major economic class asset and liabilities which IPSAS includes in (1) above)
4. A series of sub-analysis tables
 - Table 1: Revenues
 - Table 2: Expenses
 - Table 3: Transactions in assets and liabilities
 - Table 4: Holding gains and losses
 - Table 5: Other changes in volume of assets and liabilities
 - Table 6: Balance sheet

Table 6a:	Debt liabilities at nominal/market value
Table 6b:	Debt liabilities at face value
Table 7:	Expenditure by functions (COFOG)
Table 8a:	Transactions in financial assets and liabilities by counterpart sector
Table 8b:	Stock positions of financial assets and liabilities by counterpart sector
Table 9:	Total other economic flows in assets and liabilities
Annex 1:	Consolidation (from-whom-to-whom) tables
Annex 2:	Consistency with other macro economic statistics (national accounts)

In each table the columns require analysis by the following sectors:

- Central government (excluding Social security funds), sub-divided into:
 - Budgetary
 - Extra budgetary
 - Consolidated
- Social Security Funds
- State Governments
- Local Governments
- Consolidated for General Government
- A memorandum column including consolidated central government including Social Security Funds

It is not the purpose of this Guidance Note to explain the procedures for completion of the GFS reporting format². However, the content and structure of the IMF forms is important because it shows the consolidation structure required.

The structure of the reports is different from IPSAS financial statements (see below). However, most of the information in GFS reports is also required for IPSAS reporting, and vice versa. It is the organisation and presentation of the information that is different.

8.4 Consolidated IPSAS compliant financial statements

Published consolidated financial statements published annually by the entity and subject to independent audit are the “top level” financial report and have a key importance in achieving accountability. This is because this is the only financial report published by a controlling public sector entity (e.g. national or sub-national government) that is:

1. Issued in accordance with international standards
2. Subject to independent external audit certification
3. Comprehensively provides all of the relevant information for an understanding of the fiscal performance and status of the entity.

² Extensive supporting documentation, including instructional videos, can be found on the IMF website: www.imf.org

Consolidated financial statements should be presented in the formats prescribed in IPSAS. The consolidated financial statements are exactly the same as the formats as for the financial statements of individual entities as prescribed in IPSAS 1 and comprise:

1. Statement of financial position (balance sheet)
2. Statement of financial performance (operating statement)
3. Statement of changes in net assets/equity
4. Cash flow statement
5. A comparison of budget and actual
6. Notes including accounting policies

There are very few examples of consolidated whole of government financial statements that are consistent with IPSAS. Countries that have produced such statements include the UK, Australia, New Zealand and Switzerland³. Of these only Switzerland explicitly follows IPSAS. The other countries use national standards broadly consistent with IPSAS.

None of the countries cited above include a budget comparison in the format specified in IPSAS 24. New Zealand includes budget figures for both current and previous year, but does not indicate if this is the original or adjusted budget. There is no variance analysis or comment.

The following pages contain tables providing simplified templates for IPSAS compliant whole of government financial statements.

³ Website references are as follows:

UK - <https://www.gov.uk/government/collections/whole-of-government-accounts>;

Australia - <http://www.finance.gov.au/publications/commonwealth-consolidated-financial-statements/>;

New Zealand - <http://www.treasury.govt.nz/government/financialstatements>;

Switzerland -

https://www.bundespublikationen.admin.ch/cshop_mimes_bbl/00/0024817F68691ED3B6EE02E0D69FBB6E.pdf

Table 15: Whole of Government Statement of Financial Performance Template

Statement of Financial Performance for the Year Ended 30 June 20XX			
Description	Current year (\$ million)	Previous year (\$ million)	Notes
Revenue			
Taxation	700	650	X
Sale of goods and services	100	80	X
Interest revenue and dividends	150	160	X
Other revenue	100	85	X
<i>Total revenue from operations</i>	1,050	975	
Expenses			
Personnel expenses	450	480	X
Depreciation and amortisation	90	100	X
Interest payments	80	75	
Other operating expenses	60	55	X
Transfer payments and subsidies	120	125	X
<i>Total operating expenses</i>	800	835	
Operating balance before gains or losses	250	140	
Net gains/losses on financial instruments	65	55	X
Net gains/losses on non-financial instruments	- 25	- 10	X
<i>Total net gain/loss on assets and liabilities</i>	40	45	
Surplus/Deficit for the year	210	95	

Table 16: Whole Of Government Statement of Financial Position Template

Statement of Financial Position as at 30 June 20XX			
Description	Current year (\$ million)	Previous year (\$ million)	Notes
Assets			
Cash and Cash Equivalents	300	200	X
Receivables	100	96	X
Market securities, shares and Derivatives	280	230	X
Share (equity) Investments	120	125	X
Advances	25	20	X
Inventory	25	20	X
Other Assets	10	12	X
Tangible assets	200	150	X
Intangible assets and Goodwill	55	50	X
Total assets	1,115	903	
Liabilities			
Short term liabilities			
Current liabilities	75	90	X
Accrued expenses and deferred income	20	25	X
Short term provisions	15	18	X
Total short term liabilities	110	133	
Long term liabilities			
Long term loans and other liabilities	645	630	X
Long term provisions	30	25	X
Other long term liabilities	75	70	X
Total long term liabilities	750	725	
Total liabilities	860	858	
Net assets (= equity)	255	45	

Table 17: Cash Flow template

Statement of Cash Flows for the Year Ended 30 June 20XX			
Description	Current year (\$ million)	Previous year (\$ million)	Notes
Cash flows from operations			
Receipts			
Tax receipts	695	640	X
Sale of goods and services	100	80	X
Interest and dividend receipts	150	160	X
Other receipts	100	85	X
Total cash from operations	1,045	965	
Expenses			
Personnel payments	450	480	X
Interest payments	80	75	
Other operating payments	60	55	X
Transfer payments and subsidies	120	125	X
Total operating payments	710	735	
Net cash flow from operations	335	230	
Cash Flows from investing activities			
Disbursements			
Purchase of tangible assets	190	150	X
Purchase of shares and other securities	100	90	X
Purchase of intangible assets	15	20	X
Purchase of inventory	50	45	X
Cash paid as advances	10	10	X
Total cash disbursed to investments	365	315	
Receipts from investing activities			
Sale of tangible assets	50	50	X
Sale of shares and other securities	10	15	X
Sale of Intangible assets	10	0	X
Sale of inventory	45	25	X
Advances repaid	5	5	X
Total cash receipt from investing activities	120	95	
Net cash flow from investing activities	-245	-220	
Cash flows from financing activities			
Increase in short term liabilities	120	85	X
Decrease in short term liabilities	-135	-90	X
Increase in long term liabilities	95	110	X
Decrease in long term liabilities	-70	-95	X
Net cash flow from financing activities	10	10	
Total net Cash flow	100	20	
Opening balance of cash and equivalents	200	180	
Closing balance of cash and equivalents	300	200	

Note: figures are for illustrative purposes only

Table 18: Changes in net worth template

Statement of Changes in Net Worth for the Year Ended 30 June 20XX			
Description	Current year (\$ million)	Previous year (\$ million)	Notes
Opening net worth	45	-50	X
Surplus/Deficit for year	210	95	X
Closing net worth	255	45	

Table 19: Budget comparison template

Comparison of Budget with Actual Performance for the Year Ended 30 June 20XX					
Description	Original Budget (\$ million)	Revised Budget (\$ million)	Actual Results (\$ million)	Variance to Revised Budget (\$ million)	Notes
Revenue					
Taxation	750	720	700	-20	X
Sale of goods and services	110	100	100	0	X
Interest revenue and dividends	145	155	150	-5	X
Other revenue	120	115	100	-15	X
Total revenue from operations	1,125	1,090	1,050	-40	
Expenses					
Personnel expenses	475	470	450	-20	X
Depreciation and amortisation	90	90	90	0	X
Interest payments	90	85	80	-5	
Other operating expenses	55	60	60	0	X
Transfer payments and subsidies	125	120	120	0	X
Total operating expenses	835	825	800	-25	
Operating balance before gains or losses	290	265	250	-15	
Net gains/losses on financial instruments	50	60	65	5	X
Net gains/losses on non-financial instruments	10	20	-25	-45	X
Total net gain/loss on assets and liabilities	60	80	40	-40	
Surplus/Deficit for the year	230	185	210	25	

Notes and accounting policies

The notes should be specific to each entity, but the following general points should be observed

Accounting policies

The notes must commence with a statement of accounting policies

Notes related to items in above statements

In the above templates there is a column with a reference to notes. This is because the templates based on a “tree” approach to information - the statements are very high level with additional analysis provided in notes. The referencing system enables users to “drill down” to find the detailed information.

Other notes

Additional notes will be required to provide information as required in the various IPSAS (e.g. on contingent liabilities), or to improve understanding.

In addition to the requirements for all financial statements as listed above, certain additional information is required in consolidated financial statements as indicated below.

- The fact that these are consolidated financial statements IPSAS 1 Para 63(b)
- Non-controlling (minority) interests as presented as described in Section 6.2.1 above
- Any exceptions to the consolidation other than those allowed under IPSAS 35
- Accounting policies on consolidation relevant to an understanding of the financial statements

8.5 Consolidated interim reporting

As part of the drive to increase transparency governments may make available interim financial information. This may take several forms:

- Interim (Half yearly, quarterly) financial reports which will be in the same format as the annual audited financial statements but usually with less supporting information in the notes. Such interim reports may or may not be audited. The information should be consolidated in the same format as the annual financial statements.
- Budget execution reports showing expenditures as compared to the budget. These reports will not normally be audited. Information may need to be consolidated to enable budget comparability.
- Electronic access to a database of current financial information (e.g. data warehouse). This information will typically be in a “raw” state and it will be left to users to conduct any necessary consolidation.

Although only interim financial statements will have to comply with accounting standards, it is desirable that all reports and information are produced on a consistent basis. This will involve consolidating information where appropriate.

8.6 Consolidated management reporting

Fundamental to public sector management is public financial management. Managers within the public sector must conduct their activities to deliver the required outputs and outcomes in a manner that is economic, efficient and effective - in other words to achieve value for money in the delivery of public services. At the same time public sector managers must comply with the laws and regulations, including budget ceilings.

To achieve good management means that public sector managers require access to up-to-date, relevant and reliable finance information in a format that is appropriate to their needs. Such information may be made available to managers electronically or on paper.

It is essential that the information given to managers in electronic or paper reports is consistent with the external financial reports by which such managers will be held accountable. This means that where appropriate internal management reports will be consolidated reports using the same principles as set out in this Guidance Note and used in the preparation of financial statements.

Annex 1: Bibliography

1. Government Finance Statistics Manual 2014, IMF.
2. International Public Sector Accounting Standards, IPSAS Board.
3. Coverage and Sectorisation of the Public Sector, IMF, Paul Cotterell (IMF expert), Ethan Wiseman, Tobias Wickens, December 2006, IMF

Annex 2: Abbreviations

IAS	International Accounting Standards
COFOG	Classification of the Functions of Government
ESA	European System of National Accounting
EU	European Union
GBE	Government Business Enterprise
GFS	Government Finance Statistics
GFSM	GFS Manual
GGG	General Government Sector
IFAC	International Federation of Accountants
IFRS	International Financial Reporting Standards
IMF	International Monetary Fund
IPSAS	International Public Sector Accounting Standards
IPSASB	International Public Sector Accounting Standards Board
NPI	Not for Profit Institution
PFC	Public Financial Corporation
PFM	Public Financial Management
SNA	(UN System of National Accounts
SPE	Special Purpose Entities
UN	United Nations

Annex 3: Structured entities

Extracts from IPSAS 38

A structured entity is:

- (a) In the case of entities where administrative arrangements or legislation are normally the dominant factors in deciding who has control of an entity, an entity that has been designed so that administrative arrangements or legislation are not the dominant factors in deciding who controls the entity, such as when binding arrangements are significant to determining control of the entity and relevant activities are directed by means of binding arrangements; or
- (b) In the case of entities where voting or similar rights are normally the dominant factor in deciding who has control of an entity, an entity that has been designed so that voting or similar rights are not the dominant factor in deciding who controls the entity, such as when any voting rights relate to administrative tasks only and the relevant activities are directed by means of binding arrangements.

A structured entity is an entity that has been designed so that the conventional ways in which an entity is controlled are not the dominant factors in deciding who controls the entity. In the case of entities such as departments or ministries where administrative arrangements or legislation are often the dominant factors in deciding who has control of an entity, a structured entity is an entity that has been designed so that administrative arrangements or legislation are not the dominant factor in deciding who controls the entity. In the case of entities where voting or similar rights are normally the dominant factor in deciding who has control of an entity (which may be the case for some entities with profit objectives), a structured entity is an entity that has been designed so that voting or similar rights are not the dominant factor in deciding who controls the entity. Although binding arrangements frequently occur between public sector entities, binding arrangements are not normally the dominant factor in determining who controls an entity. Therefore the use of binding arrangements to determine the relevant activities of an entity may indicate the existence of a structured entity. Depending on the context a structured entity could be (i) an entity for which most of the activities are predetermined, with the relevant activities limited in scope but directed through binding arrangements or (ii) an entity for which any voting rights relate to administrative tasks only and the relevant activities are directed by means of binding arrangements.

AG21. A structured entity often has some or all of the following features or attributes:

- (a) Restricted activities.
- (b) A narrow and well-defined objective, such as to carry out research and development activities, provide a source of capital or funding to an entity or provide investment opportunities for investors by passing on risks and rewards associated with the assets of the structured entity to investors.

- (c) Insufficient net assets/equity to permit the structured entity to finance its activities without subordinated financial support.
- (d) Financing in the form of multiple contractually linked instruments to investors that create concentrations of credit or other risks (tranches).

AG22. Examples of entities that are regarded as structured entities include, but are not limited to:

- (a) A partnership between a government and a private sector entity that is not a joint venture, being a partnership established and directed by binding arrangements.
- (b) Securitization vehicles.
- (c) Asset-backed financings.
- (d) Some investment funds.