



New Zealand Institute of Chartered Accountants[†]

Exposure Draft No. 119

September 2009

ED 119 Proposed Amendment to NZ IFRS 3 – Scope exemption

Executive Summary

This exposure draft proposes to amend the scope of NZ IFRS 3 *Business Combinations* to provide a scope exemption for a local authority reorganisation where the assets and liabilities are transferred to a local authority from another local authority at no cost, or for nominal consideration, pursuant to legislation, ministerial directive or other externally imposed requirement.

Issued by the Financial Reporting Standards Board
New Zealand Institute of Chartered Accountants

[†] The New Zealand Institute of Chartered Accountants is the operating name for the Institute of Chartered Accountants of New Zealand, a body established under the Institute of Chartered Accountants of New Zealand Act 1996. All references to the New Zealand Institute of Chartered Accountants, or to the Institute, in this document mean the Institute of Chartered Accountants of New Zealand.

INTRODUCTION

The Financial Reporting Standards Board (FRSB) of the New Zealand Institute of Chartered Accountants is proposing to amend the scope of NZ IFRS 3 *Business Combinations* to provide a scope exemption for a local authority reorganisation where the assets and liabilities are transferred to a local authority from another local authority at no cost, or for nominal consideration, pursuant to legislation.

The background to this proposal is outlined in the Request for Comment that accompanies this ED.

AMENDMENT TO NZ IFRS 3 *BUSINESS COMBINATIONS*

Amend the description of the changes made to NZ IFRS 3 in the Introduction to NZ IFRS 3 as shown.

New text is underlined. Deleted text is struck through.

New Zealand specific changes

Public benefit entities

IN14 In adopting IFRS 3 for application as NZ IFRS 3, the following changes have been made in respect of public benefit entities. NZ IFRS 3:

- (a) does not apply to a local authority reorganisation where the assets and liabilities are transferred to a local authority from another local authority at no cost, or for nominal consideration, pursuant to legislation, ministerial directive or other externally imposed requirement. (paragraph NZ 2.1); and
- (b) contains additional definitions specific to public benefit entities ~~have been added to (Appendix A).~~

Qualifying entities

....

Insert new paragraph NZ 2.1 and renumber existing paragraph NZ 2.1 as NZ 2.2.

New text is underlined. Deleted text is struck through

SCOPE

2 This NZ IFRS applies to a transaction or other event that meets the definition of a business combination. This NZ IFRS does not apply to:

- (a) the formation of a joint venture.
- (b) the acquisition of an asset or a group of assets that does not constitute a business. In such cases the acquirer shall identify and recognise the individual identifiable assets acquired (including those assets that meet the definition of, and recognition criteria for, *intangible assets* in NZ IAS 38 *Intangible Assets*) and liabilities assumed. The cost of the group shall be allocated to the individual identifiable assets and liabilities on the basis of their relative *fair values* at the date of purchase. Such a transaction or event does not give rise to goodwill.
- (c) a combination of entities or businesses under common control (paragraphs B1–B4 provide related application guidance).

Public Benefit Entities

NZ 2.1 This NZ IFRS does not apply to a business combination arising from a local authority reorganisation.

Qualifying Entities

NZ 2.21 Entities which qualify for differential reporting concessions in accordance with the *Framework for Differential Reporting for Entities Applying the New Zealand Equivalents to International Financial Reporting Standards Reporting Regime (2005)* are not required to comply with the disclosure requirements in this Standard denoted with an asterisk (*).

Insert paragraph NZ 64.1 as shown below.

EFFECTIVE DATE AND TRANSITION

Effective date

64 This NZ IFRS shall be applied prospectively to business combinations for which the acquisition date is on or after the beginning of the first annual reporting period beginning on or after 1 July 2009. Earlier application is permitted. However, this NZ IFRS shall be applied only at the beginning of an annual reporting period that begins on or after 30 June 2007 and only when an entity complies, or has complied, with New Zealand Equivalent to International Financial Reporting Standard 1 *First-time Adoption of New Zealand Equivalents to International Financial Reporting Standards*. If an entity applies this NZ IFRS before 1 July 2009, it shall disclose that fact and apply NZ IAS 27 (as amended in 2008) at the same time.

Public Benefit Entities

NZ 64.1 *Amendments to NZ IFRS 3* inserted paragraph NZ 2.1. An entity shall apply that amendment prospectively for annual periods beginning on or after 1 July 2009. Earlier application is permitted.

Insert new definitions in Appendix A as follows.

APPENDIX A

Defined terms

Public benefit entities

local authority	In the context of this NZ IFRS, “local authority” means a regional council or territorial authority in accordance with the Local Government Act 2002.
local authority reorganisation	<p>In the context of this NZ IFRS, “local authority reorganisation” means:</p> <ul style="list-style-type: none">(a) the union of districts or regions; or(b) the constitution of a new district or region, including the constitution of a new local authority for that district or region; or(c) the abolition of a district or region, including the dissolution or abolition of the local authority for that district or region; or(d) the alteration of boundaries of any district or region; or(e) the transfer of a statutory obligation from one local authority to another; or(f) a proposal that a territorial authority assume the power of a regional council <p>where assets and liabilities are transferred to a local authority from another local authority at no cost, or for nominal consideration, pursuant to legislation, ministerial directive or other externally imposed requirement.</p>

Effective Date

It is proposed that:

- this amendment be applied prospectively for annual periods beginning on or after 1 July 2009; and
- early application of the amendment be permitted.

Insert a Basis for Conclusions for the scope exemption for a local authority reorganisation.

Basis for Conclusions – Scope exemption for a local authority reorganisation

This Basis for Conclusions – Scope exemption for a local authority reorganisation accompanies, but is not part of, NZ IFRS 3.

Introduction

NZBC1 This Basis for Conclusions summarises the considerations of the Financial Reporting Standards Board (FRSB) in reaching its conclusions on the scope exemption from NZ IFRS 3 for a local authority reorganisation. It sets out the rationale for the scope exemption and the future direction. In proposing the scope exemption, individual FRSB members gave greater weight to some factors than to others.

Rationale for scope exemption

NZBC2 In December 2007 the Australian Accounting Standards Board (AASB) amended AASB 3 *Business Combinations* as a consequence of the AASB's review of its accounting standards dealing with financial reporting by governments, government departments, and local governments. The AASB incorporated into AASB 3 the long-standing specific accounting requirements for restructures of local governments.

NZBC3 In May 2009, the International Public Sector Accounting Standards Board (IPSASB) issued ED 41 *Entity Combinations from Exchange Transactions*, with a comment date of 15 August 2009. ED 41 is based on IFRS 3 *Business Combinations* with proposed modifications so that the forthcoming International Public Sector Accounting Standard based on the ED can be applied by public sector entities.

NZBC4 Paragraph IN2 of the Introduction to ED 41 states that entity combinations which do not arise from exchange transactions, for example an amalgamation of municipalities or a restructuring of activities, will be considered in the second component of the IPSASB's entity combinations project. Paragraph IN2 goes on to explain that the reason for this scope exclusion is that the IPSASB has not yet examined in detail the specific public sector issues, and therefore the appropriate accounting treatment, which arise from these types of entity combinations.

NZBC5 Paragraph BC4 of the Basis for Conclusions further expands on this scope exclusion by explaining that entity combinations in the public sector generally do not represent an exchange transaction but rather are based on a non-exchange transaction. The former owners of the entity, if compensated, are not compensated at an amount approximately equal to the value of the entity. Because this is a public sector specific issue, entity combinations that result from non-exchange transactions have been excluded from the scope of the standard and will be dealt with in a separate project.

NZBC6 The FRSB supports the proposed scope exclusion in ED 41 relating to amalgamations of municipalities or a restructuring of activities, but only on the grounds that the IPSASB has not yet discussed the specific public sector issues that arise from these types of entity combinations.

NZBC7 The FRSB is proposing to provide an exemption from NZ IFRS 3 for a local authority reorganisation until such time as the IPSASB and the FRSB are able to consider the specific public sector issues for such entity combinations.

NZBC8 The FRSB plans to consider the appropriate accounting for a local authority reorganisation when the IPSASB proceeds with that phase of its entity combinations project. Issues to be considered at that time include:

- (i) whether there are sufficient, if any, differences between profit-oriented entities and PBEs that warrant modifications to NZ IFRS 3 for its application to a local authority reorganisation;
- (ii) whether a local authority reorganisation is an exchange or a non-exchange transaction;
- (iii) the appropriateness of the requirements of NZ IFRS 3, and therefore the accounting required, in relation to a local authority reorganisation; and
- (iv) whether a local authority reorganisation is a combination of entities under common control.