

## 4 Accounting boundaries

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## 4.1 Introduction

- 4.1.1 This chapter sets out the accounting principles and standards that should be applied in determining the accounting boundaries of the reporting entities covered by this Manual.

## 4.2 Accounting standards

- 4.2.1 The following accounting standards deal with accounting boundaries:
- IAS 27 Consolidated and Separate Financial Statements*
  - IAS 28 Investments in Associates*
  - IAS 31 Interests in Joint Ventures*
  - SIC 12 Consolidation – Special Purpose Entities*
  - SIC 13 Jointly Controlled Entities – Non-monetary Contributions by Venturers.*
  - IFRS 3 Business Combinations*

### **Applicability**

- 4.2.2 Departments shall prepare annual reports and consolidated financial statements (as defined in Chapter 5 of this Manual) covering all entities within their consolidation boundary. Executive NDPBs and trading funds shall prepare consolidated financial statements in accordance with the requirements of IAS 27, IAS 28 and IAS 31 without adaptation and interpretation.
- 4.2.3 The departmental boundary is different from the concept of a group under generally accepted accounting practice: it is based on in-year budgetary control and not on strategic control. Reporting entities that satisfy the IAS 27, IAS 28, IAS 31 and SIC 12 criteria for consolidation as subsidiary undertakings, associated undertakings or joint ventures will be accounted for in accordance with IAS 27, IAS 28 and IAS 31 only if:
- a) the entity is inside the boundary (see paragraphs 4.2.12 to 4.2.14); and
  - b) the entity is regarded as an extension of the parent entity, meaning that the parent entity exercises in-year budgetary and spending control over the entity.
- 4.2.4 If either of the above criteria are not met, then where a department has a formal investment in another public sector entity, it should be reported at historical cost, less any impairment following the guidance in chapter 11 of this Manual. Investments in other entities should be accounted for following the requirements of IAS 39 (chapter 9).
- 4.2.5 For the purposes of applying the principles of consolidation, the department will be the parent entity in departmental consolidations. The financial statements of all entities whose results are to be consolidated will generally have the same accounting reference date. The relevant authority will consider the treatment of non-coterminous reference dates if cases arise.
- 4.2.6 SIC 13 applies to non-monetary contributions in joint ventures that fall within the accounting boundary.

**Objective of IAS 27**

4.2.7 The objective of IAS 27 is to require parent undertakings to provide financial information about the economic activities of their group in consolidated financial statements. These consolidated financial statements should present the financial information of the group as a single economic entity.

**Objective of IAS 28**

4.2.8 The objective of IAS 28 is to reflect the effect of investments in associates where the reporting entity is partly accountable for the associate's activities.

**Objective of IAS 31**

4.2.9 The objective of IAS 31 is to reflect the effect of a venturer's shares in joint ventures. The IAS also deals with joint arrangements relating to operations and assets that are not entities.

**Objective of SIC 12**

4.2.10 The objective of SIC 12 is to ensure that, regardless of the equity holding and control structure, where in substance the special purpose entity is controlled by the sponsor, it should be consolidated.

**Objective of SIC 13**

4.2.11 SIC 13 requires that, where venturers make non-monetary contributions in exchange for an equity share in a jointly controlled entity, the venturer recognises in profit and loss the element of any gain or loss that is attributable to the equity interests of the other venturers, except in specific circumstances.

**The departmental accounting boundary**

4.2.12 In addition to reportable activities, the following reporting entities are outside the departmental resource accounting boundary:

- a) any body classified as a public corporation by the Office for National Statistics (which includes trading funds);
- b) trading funds not classified as public corporations;
- c) any body classified to the local government sector by the Office for National Statistics;
- d) NHS Trusts, NHS Foundation Trusts, and HSS Trusts;
- e) Executive non-departmental public bodies (NDPBs) (including Advisory and Tribunal NDPBs) that produce their own financial statements, except where there are good grounds for consolidation as determined by the relevant authority;
- f) other public bodies where the department exercises only strategic control, except where there are good grounds for consolidation as determined by the relevant authority; and
- g) any body classified to the private or rest of the world sectors by the Office for National Statistics.

4.2.13 The departmental resource accounting boundary will, therefore, include the following entities:

- a) Supply-financed agencies;
- b) non-agency parts of the department accounted for through the Supply process and other bodies whose expenditure is accounted for in separate financial statements, including non-executive NDPBs such as Advisory NDPBs and Tribunal NDPBs;
- c) exceptionally, executive NDPBs or other public bodies that produce their own financial statements where there are good grounds for consolidation as determined by the relevant authority; and
- d) Strategic Health Authorities and Primary Care Trusts in England, Local Health Boards in Wales, and Health Boards in both Scotland and Northern Ireland.

4.2.14 The criteria set out above relating to the exceptional consolidation of executive NDPBs and other public bodies that produce their own financial statements will apply to very few entities, and should be agreed with the relevant authority on a case by case basis. A minimum requirement for consolidation will be that the department has the power to exercise direct in-year budgetary control over expenditure, for example, by amending previously agreed budgets for all or any part of the NDPB's expenditure and to require any further expenditure by the NDPB to comply with the amended budgets. Entities should refer to the relevant authority in cases where any of the requirements cannot be applied or there is uncertainty as to how they are to be applied.

## **IFRS 3 Business Combinations**

### ***Applicability***

4.2.15 IFRS 3 excludes from its scope business combinations involving entities or businesses under common control. Public sector bodies are deemed to be under common control. The combination of two or more public sector bodies into one new body, or the transfer of functions from the responsibility of one part of the public sector to another, will be accounted for using merger accounting as detailed below.

4.2.16 IFRS 3 applies to all combinations involving an entity or entities within the public sector with an entity outside the sector.

### ***Objective of IFRS 3***

4.2.17 The objective of IFRS 3 is to specify that all business combinations (except those excluded from its scope) should be accounted for using the purchase method (also known as the acquisition method). IFRS 3 requires that all such combinations be accounted for at fair value at the date of the combination and that goodwill arising from such transactions is accounted for as an asset. Goodwill is not amortised but subject to impairment testing as required by IAS 36 *Impairment of Assets*.

### ***Merger accounting***

4.2.18 The carrying value of the assets and liabilities of the combining bodies or functions are not adjusted to fair value on consolidation. Appropriate adjustments should be made to achieve uniformity of accounting policies in the combining bodies.

4.2.19 The results and cash flows of all the combining bodies (or functions) should be brought into the financial statements of the combined body from the beginning of the financial year in which the combination occurred, adjusted to achieve uniformity of accounting policies. The corresponding figures should be restated by including the results for all the combining bodies (or functions) for the previous period and their

statement of financial position for the previous statement of financial position date, adjusted as necessary to achieve uniformity of accounting policies.

- 4.2.20 For all such adjustments required to achieve uniformity of accounting policies, the double entry will be to the General Fund (or equivalent).

### ***Disclosure***

- 4.2.21 A reporting entity that receives a transfer of functions should disclose in its financial statements that the transfer has taken place (including a brief description of the transferred function), giving the date of the transfer, the name of the transferring body and the effect on the financial statements.

- 4.2.22 A reporting entity that transfers functions to another reporting entity should provide the same information about the transfer in its financial statements.

### ***Other requirements***

- 4.2.23 Transfers of fixed assets that are not machinery of government changes<sup>1</sup> or part of a transfer of functions should be transferred at fair value following the fair value measures in IFRS 3.

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<sup>1</sup> Machinery of Government changes are those changes that transfer responsibility for a function from one part of the public sector to another.