SECTION PS 2500
basic principles of consolidation

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PURPOSE AND SCOPE

.01 This Section establishes standards on the basic principles of consolidation involved in preparing government financial statements as required by GOVERNMENT REPORTING ENTITY, paragraph PS 1300.27. Additional consolidation issues, such as accounting for governmental units with non-controlling interests, acquisitions and sales of government investments in governmental units, and accounting for the change in status of a governmental unit to a government business enterprise, are dealt with in ADDITIONAL AREAS OF CONSOLIDATION, Section PS 2510.

.02 Government financial statements are the financial statements of the government reporting entity. The government reporting entity, defined in GOVERNMENT REPORTING ENTITY, paragraph PS 1300.07, comprises government components and those organizations that are controlled by the government. Government organizations include government business enterprises, government not-for-profit organizations and other government organizations. [Former paragraph PS 2500.02, amended by 2018-2019 annual improvements, retained in Archived Pronouncements.]

.02A Section PS 1300 requires that governmental units are consolidated in the financial statements and government business enterprises are included in the financial statements on a modified equity basis. Governmental units are included in a government's financial statements after their accounting policies have been conformed to those of the government. A similar adjustment is not required when including government business enterprises in the financial statements because under the modified equity method the accounting policies of a government business enterprise are not conformed to those of the government. The chart included as Appendix A to this Section outlines this government reporting entity framework in more detail.

.03 This Section does not deal with accounting for:

(a) government business enterprises (see INVESTMENTS IN GOVERNMENT BUSINESS ENTERPRISES, Section PS 3070); or

(b) portfolio investments (see PORTFOLIO INVESTMENTS, Section PS 3041).

DEFINITIONS

.04 The following definitions have been adopted for the purposes of this Section:

(a) A **government organization** is any organization controlled by a government that is a separate entity with the power to contract in its own name and that can sue and be sued. (Control is explained in GOVERNMENT REPORTING ENTITY, paragraphs PS 1300.07-.24.)

(b) A **government business enterprise** is a government organization that has all of the following characteristics:

(i) it is a separate entity with the power to contract in its own name and that can sue and be sued;

(ii) it has been delegated the financial and operational authority to carry on a business;

(iii) it sells goods and services to individuals and organizations outside of the government reporting entity as its principal activity; and

(iv) it can, in the normal course of its operations, maintain its operations and meet its liabilities from revenues received from sources outside of the government reporting entity.

These criteria are explained in GOVERNMENT REPORTING ENTITY, paragraphs PS 1300.29-.31.

(c) A **government not-for-profit organization** is a government organization that has all of the following characteristics:

(i) It is a separate entity with the power to contract in its own name and that can sue and be sued.

(ii) It has counterparts outside the public sector as defined in paragraph .02 of Introduction to the Public Sector Accounting Handbook. [Former paragraph PS 2500.04(c)(ii), amended by the Conceptual Framework, retained in Archived Pronouncements.]

(iii) It is an entity normally without transferable ownership interests.

(iv) It is an entity organized and operated exclusively for social, educational, professional, religious, health, charitable or any other not-for-profit purpose.

(v) Its members, contributors and other resource providers do not, in such capacity, receive any financial return directly from the organization.

(d) **Government financial statements** are financial reports 1 published by a government that report on the financial position and changes in financial position of the government reporting entity through the consolidation of its governmental units and inclusion of its investments in government business enterprises on a modified equity basis. [Former paragraph PS 2500.04(d), amended by 2022-2023 remaining annual improvements, retained in Archived Pronouncements.]

(e) A **governmental unit** is a government component, 2 government not-for-profit organization or other government organization. Government business enterprises are not governmental units. [Former paragraph PS 2500.04(e) related footnote, amended by the Conceptual Framework, retained in Archived Pronouncements.]

(f) **Internal charges** are charges between governmental units, such as cost allocations or service charges for the use of assets or the provision of services.

[Former paragraphs PS 2500.04(a)-(e), amended by 2018-2019 annual improvements, retained in Archived Pronouncements.]

BASIC PRINCIPLES

.05 The purpose of government financial statements is to present the effects of transactions of the government reporting entity, as defined in GOVERNMENT REPORTING ENTITY, Section PS 1300, with organizations and individuals external to that entity, taking into consideration the accounting for government business enterprises described in INVESTMENTS IN GOVERNMENT BUSINESS ENTERPRISES, Section PS 3070. 3 [Former paragraph PS 2500.05, amended by 2018-2019 annual improvements, retained in Archived Pronouncements.]

.06 *Government financial statements should consolidate governmental units* 4 *line-by-line on a uniform basis of accounting after eliminating inter-governmental unit transactions and balances.* [MAY 1999]

.07 The basic steps of consolidation required by paragraph PS 2500.06 are as follows:

(a) The accounting policies of governmental units are conformed to those of the government.

(b) The balances of assets, liabilities and accumulated surplus / deficit of the governmental units, after being adjusted in accordance with (a), are added together and included on the consolidated statement of financial position for the government reporting entity. The assets and liabilities are accounted for in government financial statements at their carrying value in the records of the governmental units being consolidated, taking into account the adjustments required in (a).

(c) The revenues and expenses of the governmental units, after being adjusted in accordance with (a), are added together and the current and the most recent prior period aggregated amounts would be reported on the consolidated statement of operations and the consolidated statement of changes in net assets or net liabilities. [Former paragraph PS 2500.07(c), amended by FINANCIAL STATEMENT PRESENTATION, Section PS 1202, retained in Archived Pronouncements.]

(d) The effects of inter-governmental unit transactions on assets, liabilities, accumulated surplus / deficit, revenues and expenses are eliminated, as described in paragraphs PS 2500.08-.18.

(e) Governmental units are included in government financial statements from the date of their creation or the date they became eligible for inclusion, and are removed from those financial statements from the date of their sale or other form of disposition or dissolution. If a governmental unit becomes eligible for inclusion as a result of a reinterpretation of existing circumstances, it would be included in the financial statements as if it had always been part of the government reporting entity. Such circumstances would, therefore, involve a restatement of comparative numbers. Accounting for the circumstances when a governmental unit changes in status to become a government business enterprise is dealt with in ADDITIONAL AREAS OF CONSOLIDATION, paragraphs PS 2510.42-.51.

.08 Eliminating the effects of inter-governmental unit transactions ensures that the consolidated accounts do not overstate or understate assets, liabilities, accumulated surplus / deficit, revenues and expenses because of inter-governmental unit transactions. Therefore, consolidation eliminations are required to remove the following effects of transactions between governmental units:

(a) inter-governmental unit assets and liabilities, including any investments in governmental units recorded by other governmental units in the form of shares or contributed surplus; 4

(b) inter-governmental unit revenues and expenses, including transfers, and internal charges as described in paragraphs PS 2500.09-.14;

(c) inter-governmental unit dividends, if any, that have been declared; and

(d) unrealized inter-governmental unit gains and losses, including those related to inter-governmental unit sales or transfers of tangible capital assets, as described in paragraph PS 2500.18.

Inter-governmental unit revenues and expenses

.09 The consolidation eliminations relating to inter-governmental unit revenues and expenses would vary depending on whether expenses are presented by function or by object. The presentation of expenses by both function and object in the financial statements may require two different sets of elimination entries. However, the need for elimination entries will vary depending on how inter-governmental unit transactions are recorded.

.10 The total expenses reported by function should be equal to the total expenses disclosed by object. Consistent with paragraph PS 2500.05, consolidated revenues should not be created, increased or decreased as a result of inter-governmental unit transactions.

Functional presentation of expenses on the statement of operations

.11 FINANCIAL STATEMENT PRESENTATION, Section PS 1202, requires that a government's expenses of the accounting period be reported on the statement of operations by function or major program. Reporting by function or major program is recommended because this information shows users the purposes for which goods and services have been acquired or consumed and helps them assess the allocation of resources to government functions or programs. [Former paragraph PS 2500.11, amended by FINANCIAL STATEMENT PRESENTATION, Section PS 1202, retained in Archived Pronouncements.]

.12 The objectives of functional reporting are achieved in a government's financial statements when inter-governmental unit expenses are included in the expenses of the governmental unit that ultimately bears the cost and, therefore, the ultimate accountability for that cost.

.13 Depending on how a governmental unit records internal charges to other governmental units, inter-governmental unit revenues may need to be eliminated to achieve the objectives of paragraph PS 2500.10. For example, for a functional presentation:

(a) If the originating governmental unit records revenue from internal charges, an elimination entry would be required to eliminate such revenue against the related expense in that originating governmental unit.

(b) In contrast, if the originating governmental unit records a recovery of an expense from internal charges, no elimination entry would be required. The expenses and recovery of expenses would offset each other in the accounts of the originating governmental unit.

Disclosure of expenses by object in the notes to the financial statements

.14 FINANCIAL STATEMENT PRESENTATION, Section PS 1202, requires that a government's expenses be disclosed by object. The objective of disclosure of expenses by object is to provide information that is useful in evaluating the economic impact of government acquiring or consuming various types of resources. For the purposes of preparing such disclosure, expenses would reflect the resources acquired by the originating governmental unit, such as employees' salaries, goods and services and tangible capital assets. [Former paragraph PS 2500.14, amended by FINANCIAL STATEMENT PRESENTATION, Section PS 1202, retained in Archived Pronouncements.]

Unrealized gains and losses on inter-governmental unit sales or transfers of assets

.15 *Inter-governmental unit gains and losses arising on the sale or transfer of assets and liabilities remaining within the government reporting entity should be eliminated.* [Former paragraph PS 2500.15 retained in Archived Pronouncements.] [APRIL 2012]

.16 Unless items measured at cost or amortized cost are transferred at their carrying value, elimination of unrealized inter-governmental gains and losses on the sale or transfer of assets and liabilities is required to ensure the consolidated financial statements are presented in accordance with paragraph PS 2500.05. [Former paragraph PS 2500.16 retained in Archived Pronouncements.]

.16A Operating gains and losses associated with inter-governmental unit sales or transfers of financial instrument assets and financial instrument liabilities in the fair value category require elimination. When the related instrument is still held within the consolidated entity, an adjustment is required to eliminate a gain or loss as it is unrealized. To accomplish this, the gain or loss is reclassified from the consolidated statement of changes in net assets or net liabilities in the accumulated remeasurement gains and losses component. [Former paragraph PS 2500.16A, amended by FINANCIAL STATEMENT PRESENTATION, Section PS 1202, retained in Archived Pronouncements.]

.17 The existence of unrealized inter-governmental unit losses may indicate a decline in the value of assets. When a loss is attributed to impairment or a permanent decline in value, it is reported in the statement of operations. [Former paragraph PS 2500.17 retained in Archived Pronouncements.]

Tangible capital assets

.18 A government is required to report tangible capital assets in accordance with FINANCIAL STATEMENT PRESENTATION, Section PS 1202. Those standards require that the net book value of the government's tangible assets be reported as non-financial assets on the statement of financial position. The consumption of tangible capital assets must be recognized as an expense in the government's statement of operations. So, in a government's financial statements, adjustments would need to be made to ensure that the assets are presented at historical cost to the government reporting entity, as follows:

(a) The amount reported for tangible capital assets on the government's consolidated statement of financial position would exclude any unrealized inter-governmental unit gains and losses arising on the sale or transfer of tangible capital assets and the portion of accumulated amortization attributable to such inter-governmental unit gains and losses on tangible capital assets.

(b) The amortization of tangible capital assets recognized in the expenses reported on a government's consolidated statement of operations would be adjusted to eliminate the portion of the amortization charges attributable to unrealized inter-governmental unit gains and losses arising on the sale or transfer of tangible capital assets.

(c) In a government's disclosure of tangible capital assets in the notes or schedules to its financial statements, the cost and amortization amounts reported for tangible capital assets would exclude any unrealized inter-governmental unit gains and losses arising on the sale or transfer of tangible capital assets and any related effect of such gains and losses on amortization amounts.

[Former paragraph PS 2500.18, amended by FINANCIAL STATEMENT PRESENTATION, Section PS 1202, retained in Archived Pronouncements.]

Statements at different dates

.19 A difference in fiscal periods of a government reporting entity and a governmental unit does not justify the exclusion of the governmental unit from consolidation. Normally the governmental unit can prepare for consolidation purposes, statements for a period that exactly or nearly coincides with the fiscal period of the government reporting entity.

.20 *When, for purposes of consolidation, it is not possible to use governmental unit financial statements for a period that substantially coincides with that of the government's financial statements, this fact, and the period covered by the governmental unit financial statements used, should be disclosed.* [MAY 1999]

.21 *When the fiscal periods of a government reporting entity and a governmental unit are not the same, events relating to or transactions of the governmental unit that have occurred during the intervening period and significantly affect the financial position or results of operations of the government reporting entity should be recorded in the government's financial statements.* [MAY 1999]

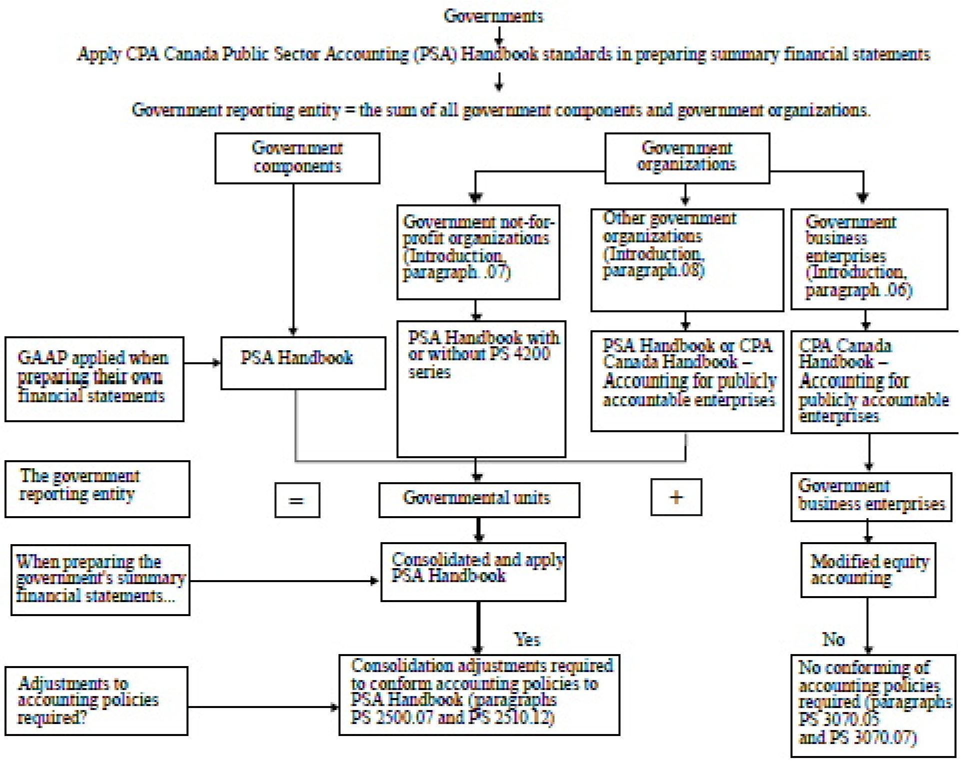
EFFECTIVE DATE AND TRANSITIONAL PROVISIONS

.22 FINANCIAL STATEMENT PRESENTATION, Section PS 1202, issued in October 2023, amended paragraphs PS 2500.07(c), PS 2500.11, PS 2500.14, PS 2500.16A and PS 2500.18. The amendments are applicable at the same time as Section PS 1202, for fiscal years beginning on or after April 1, 2026. Earlier adoption is permitted if Section PS 1202 is also early adopted. Prior period amounts would need to be restated to conform to the requirements for comparative financial information in Section PS 1202.

APPENDIX A

GOVERNMENT REPORTING ENTITY FRAMEWORK

This Appendix is illustrative only and matters of principle relating to particular situations should be decided in the context of the Introduction and the standards referenced in the diagram. While illustrative, this Appendix is a primary source of GAAP, as identified in GENERALLY ACCEPTED ACCOUNTING PRINCIPLES, paragraph PS 1150.03(d)(iii).



[Former Appendix A, amended by 2018-2019 annual improvements, retained in Archived Pronouncements.]

Footnotes

1. Refer to Figure 3.1 in Chapter 3 of the Conceptual Framework, where financial statements are identified as an important type of financial report.

2. A government component is defined in the Introduction to the Public Sector Accounting Handbook.

3. Transactions and balances between governmental units and government business enterprises are not eliminated because government business enterprises are not consolidated. They are accounted for in government financial statements by the modified equity method. This method does not require the elimination of intra-government reporting entity transactions and balances (see INVESTMENTS IN GOVERNMENT BUSINESS ENTERPRISES, Section PS 3070). All unrealized gains and losses arising from transactions between governmental units and government business enterprises that remain within the reporting entity are, however, required to be eliminated.

4. Governments normally create governmental units, often through a restructuring of existing government resources, rather than acquire them. Accounting for acquired governmental units is dealt with in ADDITIONAL AREAS OF CONSOLIDATION, paragraphs PS 2510.11-.32.

4. When government financial statements are prepared, the investment account of the government is replaced by the identifiable assets and liabilities of the governmental unit. Many governmental units, however, are not "investments" of the government but, instead, are departments or agencies or funds that are integral to and derive their sole purpose from the legal or legislative responsibilities of government. In addition, many governmental units do not even issue share capital.