

## Basis for Conclusions on AASB 2013-5 and dissenting views

*This Basis for Conclusions accompanies, but is not part of, AASB 10. The Basis for Conclusions was originally published with AASB 2013-5 Amendments to Australian Accounting Standards – Investment Entities.*

BC1 This Basis for Conclusions summarises the Australian Accounting Standards Board’s (AASB) considerations in issuing AASB 2013-5 *Amendments to Australian Accounting Standard – Investment Entities*. Individual Board members gave greater weight to some factors than to others.

### Background

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BC2 AASB 2013-5 is the result of the AASB’s due process, which began when the AASB issued Exposure Draft ED 220 *Investment Entities* (AASB ED 220) in September 2011 (incorporating International Accounting Standards Board [IASB] ED/2011/4 *Investment Entities*). That Exposure Draft proposed that an investment entity be required to account for investees that it controls at fair value through profit or loss, rather than consolidate them.

BC3 In the material accompanying ED 220, AASB members expressed concerns with the ED/2011/4 proposals, including:

- (a) the exception to consolidation goes against the application of the well-established accounting concept of control, which is designed to result in the presentation of all the assets, liabilities, income and expenses of the group, and the amendments would result in a loss of relevant information for users of financial statements;
- (b) the basis of the exception to consolidation is the type of entity, rather than the underlying relationship between investors and investees; and
- (c) there are no clear principles underpinning the classification of entities as investment entities and the criteria for identifying investment entities are rule-based and open to opportunistic behaviour.

BC4 As evident from the responses to ED 220, views were divided among Australian constituents. Some expressed concerns similar to those of the AASB members. However, others expressed broad support for requiring some types of entities to account for controlled investees at fair value through profit or loss, rather than having them consolidate such entities.

BC5 The AASB expressed its concerns in its submission to the IASB on IASB ED/2011/4.

BC6 In October 2012, the IASB amended IFRS 10 *Consolidated Financial Statements*, IFRS 12 *Disclosures of Interest in Other Entities* and IAS 27 *Separate Financial Statements* for investment entities to provide an exception to consolidating particular subsidiaries for investment entities, requiring them instead to measure their investments in unconsolidated subsidiaries at fair value through profit or loss.

BC7 The AASB noted that its concerns with the ED/2011/4 proposals were not adequately addressed in the IASB amendments. The AASB also considered the disclosures required by the IASB amendments and noted that they require an investment entity to provide information about the exception to consolidation rather than addressing the loss of consolidation information that preparing a complete set of consolidated general purpose financial statements would provide.

BC8 Because of its concerns with the IASB amendments, the AASB decided to undertake further due process. After considering a number of different possible approaches to the recognition and measurement of controlled investees of investment entities, including (i) consolidation and (ii) fair value measurement with compensating disclosures, the AASB issued ED 233 *Australian Additional Disclosures – Investment Entities* in December 2012. It proposed to introduce the exception to consolidation for investment entities (as per the IASB amendments) and to require Australian additional disclosures for Australian entities that meet the IASB’s investment entity criteria. The Australian additional disclosures proposed in ED 233 were in the form of:

- consolidated financial statements prepared in a manner consistent with the definition of consolidated financial statements in Appendix A of AASB 10 *Consolidated Financial Statements*; and
- a summary of the significant accounting policies used in preparing those consolidated financial statements that are not otherwise disclosed in accordance with AASB 101 *Presentation of Financial Statements*.

- BC9 ED 233 also specifically asked respondents whether they have any alternative approaches/disclosure strategies that can be employed to minimise the adverse impact on the decision-making of the loss of consolidation information.
- BC10 The AASB received 29 submissions on ED 233. The vast majority of respondents did not support the proposed Australian additional disclosures. These respondents expressed support for introducing the IASB amendments without Australian additional disclosures.
- BC11 The AASB staff also conducted targeted outreach with users of financial statements and the limited feedback received indicated that if there were to be Australian additional disclosures required, an example of the information that would be relevant is information about the earnings and liabilities of subsidiaries of investment entities.

## **AASB deliberations on adopting the IASB amendments in Australia without Australian additional disclosures**

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- BC12 The AASB considered three main approaches to introducing the IASB amendments for investment entities in Australia:
- A. issue the IASB amendments without Australian additional disclosures;
  - B. issue the IASB amendments with Australian additional disclosures as proposed in AASB ED 233; and
  - C. issue the IASB amendments with Australian additional disclosures that are reduced compared with the ED 233 proposals, in particular, disclosures about an unconsolidated subsidiary's total assets, total liabilities and total comprehensive income.
- BC13 The AASB considered and rejected the approach of not adopting the IASB's amendments for Australian investment entities as this would result in Australian investment entities not being able to assert IFRS compliance, an outcome that would be contrary to the AASB's policy of having "... Tier 1 for-profit entities being IFRS compliant"<sup>2</sup>.
- BC14 The majority of AASB members expressed a preference for, or could at least accept, Approach A, consistent with the AASB's policy of IFRS adoption. Some members consider that the fair value of controlled entities can arguably be regarded as more relevant for users of financial statements of investment entities than consolidation information. Some other members consider that the IASB's criteria for determining investment entities lack rigour and could lead to inconsistent application. However, on balance, the majority of members are willing to accept, in the absence of evidence to the contrary, that the IASB amendments, including the disclosures required of investment entities in accordance with IFRS 12, would be sufficient to meet the needs of users of financial statements of investment entities, consistent with the feedback received from the vast majority of the respondents to ED 233.
- BC15 This majority of AASB members could not accept Approach C as there was insufficient feedback from users to suggest that the reduced disclosures proposed in Approach C would be useful. Those AASB members did not think it appropriate to delay adoption while further input from users is sought.
- BC16 The AASB noted the wide range of arguments put forward by respondents to ED 233 for favouring Approach A including the view that fair value information is most relevant for investors of investment entities in many circumstances; and the cost to Australian preparers of financial statements compared with other jurisdictions of providing Australian additional disclosures. However, despite accepting Approach A, the AASB did not accept all of those arguments. In particular, the AASB did not accept the arguments that requiring Australian additional disclosures would reduce comparability (as distinct from uniformity) between Australian investment entities and their international counterparts or would lead to the perception that Australian investment entities are not IFRS compliant.
- BC17 On balance, the AASB decided to adopt Approach A. This was on the basis that the AASB would monitor the implementation of the IASB amendments for Australian investment entities. This would include monitoring the disclosures made in accordance with AASB 12 *Disclosure of Interests in Other Entities* and AASB 101 *Presentation of Financial Statements* paragraph 17(c)<sup>3</sup>. Such monitoring, which may be via a post-implementation review, would be undertaken with a view to potentially adding Australian additional disclosure requirements at a later stage, if it were to become evident that additional disclosures are warranted, noting that such disclosures might be different from those proposed in ED 233 or Approach C. Monitoring

<sup>2</sup> AASB Policy Statement *Policies and Processes* March 2011, paragraph 7

<sup>3</sup> AASB 101 paragraph 17(c) requires an entity to provide additional disclosures when compliance with the specific requirements in Australian Accounting Standards is insufficient to enable users to understand the impact of particular transactions, other events and conditions on the entity's financial position and financial performance.

might also lead to the AASB deciding to write to the IASB, informing it of the findings and concerns arising from the Australian experience.

## **GAAP/GFS Harmonisation**

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- BC18 In adopting Approach A, the AASB considered whether there would be any GAAP/GFS harmonisation implications that it would need to address in the context of AASB 1049 *Whole of Government and General Government Sector Financial Reporting*. The AASB noted that no such implications are expected to arise because, although the whole of government or general government sector might be a parent of an investment entity, the whole of government and general government sector would not themselves be investment entities.

## **Application to Tier 2**

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- BC19 The AASB noted that the way in which the IASB has defined an investment entity (including that such an entity need not have more than one investor) could result in there being investment entities that do not have public accountability as defined in Appendix A of AASB 1053 *Application of Tiers of Australian Accounting Standards* and are therefore eligible to present Tier 2 general purpose financial statements.
- BC20 In addition, the AASB considered the entities listed in Appendix B of AASB 1053 that are deemed to have public accountability. Whilst many investment entities would fall within the list of deemed entities, there could be a number of investment entities that would not be captured – for example, managed investment schemes that are investment entities but are not registered and therefore, again potentially eligible to present Tier 2 general purpose financial statements.
- BC21 The AASB conducted due process on whether Tier 2 investment entities should be provided with any relief from the disclosures required by the IASB amendments through ED 220.
- BC22 After considering constituent feedback, the AASB decided the disclosures in the IASB amendments for investment entities should be applied to both Tier 1 and Tier 2 investment entities as it considers those disclosures to be fundamental to the needs of users in decision-making. Accordingly, the AASB decided that it would not be appropriate to exempt those investment entities from any of the disclosures in the IASB amendments.

## **Dissenting views**

### **Dissent of Peter Gibson, Jayne Godfrey, John O’Grady and Kevin M. Stevenson**

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- DO1 In our opinion the exception to consolidation for investment entities that requires controlled investees to be measured at fair value through profit or loss rather than being consolidated is a violation of the basic principle that an entity should account for all of its assets, liabilities, income and expenses.
- DO2 At the most fundamental level we do not see the provision of fair value information for investments as a substitute for, or an alternative to, consolidated information. Without the detailed consideration of that part of the financial position and financial performance of an entity represented by its controlled entities, fair value movements would not be sufficient for decision-making and offset too much information into a single line item.
- DO3 We regard the exception as fundamentally based on a view that an entity’s business model should determine accounting treatments. However, we do not believe that an entity’s business model should drive how it accounts for its controlled investees. In our opinion, the business model approach and the IASB’s criteria for determining investment entities, which we believe lack rigour, will lead to uncertainty in application and inconsistency of reporting between similar entities. This approach also has the potential to promote structuring opportunities to avoid consolidation. In turn, this would be to the detriment of providing useful, comparable information to users of financial statements.
- DO4 We believe that providing exceptions to principles further complicates accounting, introduces unjustified complexity to financial statements and reduces comparability of entities’ financial reports across sectors. It also creates a precedent for further, less rigorous standard-setting.

- DO5 For Australia, the exception to consolidation would require de-consolidation of controlled entities when Australia has been well-served by the control principle and has been relatively free of criticism of off-balance-sheet accounting.
- DO6 Additionally, we have not heard from users of financial statements of investment entities in Australia that consolidation information is not useful or relevant for decision-making.
- DO7 Furthermore, if the fair values of controlled investments held by investment entities are relevant, we are of the view that they could be provided as supplementary disclosures in financial statements, consistent with the disclosure requirements in AASB 7 Financial Instruments: Disclosures for financial instruments with carrying amounts that differ from their fair value.