

Investment entities and subsidiaries

The Committee received a request regarding the investment entity requirements in IFRS 10, including how an entity applies the requirements in paragraphs 27 and 28 of IFRS 10, and how an investment entity assesses whether it consolidates a subsidiary applying paragraph 32 of IFRS 10 in specified circumstances. The Committee discussed the following questions:

- a. does an entity qualify as an investment entity if it possesses all three elements described in paragraph 27 of IFRS 10, but does not have one or more of the typical characteristics of an investment entity listed in paragraph 28 of IFRS 10? (Question a)
- b. does an entity provide investment management services to investors (as specified in paragraph 27(a) of IFRS 10) if it outsources the performance of these services to a third party? (Question b).
- c. to what extent can an investment entity provide investment-related services, itself or through a subsidiary, to third parties? (Question c)
- d. does a subsidiary provide services that relate to its parent investment entity's investment activities (as specified in paragraph 32 of IFRS 10) by holding an investment portfolio as beneficial owner? (Question d)

Question a

Paragraph 27 of IFRS 10 lists the three elements an entity must possess to qualify as an investment entity. Paragraph B85A of IFRS 10 emphasises the importance of considering all facts and circumstances when assessing whether an entity is an investment entity, and notes that an entity that possesses the three elements of the definition of an investment entity in paragraph 27 is an investment entity. Paragraphs B85B-B85M then describe the elements of the definition in more detail.

Paragraph 28 of IFRS 10 lists typical characteristics that an entity considers in assessing whether it possesses all three elements in paragraph 27, and says that the absence of any of these characteristics does not necessarily disqualify an entity from being an investment entity. Paragraph B85N of IFRS 10 clarifies that the absence of one or more of the typical characteristics of an investment entity listed in paragraph 28 of IFRS 10 indicates that additional judgement is required in determining whether the entity is an investment entity.

Accordingly, the Committee concluded that an entity that possesses all three elements of the definition of an investment entity in paragraph 27 of IFRS 10 is an investment entity. This is the case even if that entity does not have one or more of the typical characteristics of an investment entity listed in paragraph 28 of IFRS 10.

Question b

Paragraph 27(a) of IFRS 10 requires an investment entity to provide investors with investment management services. IFRS 10 does not specify how the investment entity must provide these services, and does not preclude it from outsourcing the performance of these services to a third party.

Accordingly, the Committee concluded that an investment entity responsible for providing investment management services to its investors can engage another party to perform some or all of these services on its behalf (ie it can outsource the performance of some or all of these services).

Question c

Paragraph 27(b) of IFRS 10 requires that the business purpose of an investment entity is to invest solely for capital appreciation, investment income, or both. Paragraph B85C of IFRS 10 says that an investment entity may provide investment-related services, either directly or through a subsidiary, to third parties as well as to its investors (even if those activities are substantial to the entity), subject to the entity continuing to meet the definition of an investment entity.

Accordingly, the Committee concluded that an investment entity may provide investment-related services to third parties, either directly or through a subsidiary, as long as those services are ancillary to its core investing activities and thus do not change the business purpose of the investment entity.

The Committee observed that an investment entity assesses whether the investment management services provided by a subsidiary, including those provided to third parties, relate to the investment entity's investment activities. If so, the investment entity includes these services when assessing whether the investment entity itself possesses the element of the investment entity definition in paragraph 27(b) of IFRS 10.

The Committee also noted that, applying paragraph 32 of IFRS 10, an investment entity consolidates any non-investment entity subsidiaries whose main purpose and activities are providing services that relate to the investment entity's investment activities.

Question d

The Committee observed that it had previously discussed a question similar to Question d. At its meeting in March 2014, the Committee issued an agenda decision noting its conclusion that a subsidiary does not provide investment-related services or activities if the subsidiary holds investments for tax optimisation purposes and there is no activity within the subsidiary.

Similarly, the Committee concluded that an investment entity does not consider the holding of investments by a subsidiary as beneficial owner (and recognised in the subsidiary's financial statements) to be a service that relates to the parent investment entity's investment activities (as specified in paragraph 32 of IFRS 10).

For all four questions (ie Questions a—d), the Committee concluded that the principles and requirements in IFRS Standards provide an adequate basis for an entity to determine the appropriate accounting in each of the specified circumstances. Consequently, the Committee decided not to add this matter to its standard-setting agenda.