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International
Accounting Standards
Board

INFORMATION FOR OBSERVERS

Board Meeting:	**November 2008, London**
Project:	**Consolidation**
Subject:	**Disclosure (Agenda paper 16D)**

INTRODUCTION

Objective of this paper

1 The objective of this paper is to review outstanding issues relating to disclosure proposals for inclusion in the exposure draft of the IFRS to replace IAS 27 *Consolidated and Separate Financial Statements* and SIC-12 *Consolidation –Special Purpose Entities.*

2 In relation to consolidated entities, we propose disclosure requirements that enable users to evaluate:

(a) the structure of the group; and

(b) the nature and financial effect of restrictions on assets and liabilities that are a consequence of those assets and liabilities being held by subsidiaries.

3 Disclosure requirement 2 (b) is similar to existing disclosure requirements in IAS 27, which require a reporting entity to disclose the nature and extent of any significant restrictions on the ability of subsidiaries to transfer funds to the parent. It is also consistent with the disclosure requirements proposed in FASB's exposure draft of amendments to FIN 46(R) *Consolidation of Variable Interest Entities*.

4 At this meeting we seek a decision from the Board on whether you agree that the disclosure requirements proposed should be included in the exposure draft.

DISCLOSURE REQUIREMENTS

General considerations

5 Consolidation is the process by which the financial statements of a parent are combined with those of its subsidiaries, as a single economic entity. Consolidated financial statements are considered to be beneficial to users of financial statements in the decision-making process. We believe, however, that there is a case for providing some disaggregated information.

6 Various bodies representing users of financial statements have expressed concern that consolidated financial statements do not provide users with adequate financial information and transparency.

7 Staff at the Canadian Accounting Standards Board summed up the concerns of its User Advisory Council as follows:[1]

> Consolidated financial statements do not provide sufficient financial information for a wide range of users to understand the relationships between the assets and liabilities of a parent company and its subsidiaries, or restrictions on the availability of a subsidiary's assets and cash flows to its parent company.[2]

The structure of the group

Proposed disclosure requirement

8 We propose that a parent be required to disclose information about the structure and activities of the group, including a list of individually material subsidiaries providing:

(a) name and country of incorporation or residence;

(b) proportion of ownership interest and, if different, proportion of voting interest;

(c) main activity; and

(d) total assets.

Staff analysis

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[1] This body includes investment analysts, bankers, rating agencies and other users.
[2] The Canadian Accounting Standards Board's (AcSB) staff paper on Disclosure of Non-Consolidated Information (November 2007)

9 We believe that comparability of consolidated financial statements is enhanced when users of financial statements have information about the extent to which assets, liabilities, equity, revenues and expenses are managed within subsidiaries of a group.

Individually material subsidiaries

10 Information relating to individually material subsidiaries was requested by users, subsequent to its removal from IAS 27 as part of the 2003 improvements project. We believe that this disclosure provides useful information about the complexity of the group and the nature of its activities.

11 We propose that a parent be required to disclose disaggregated information relating to individually material subsidiaries including:

(a) **name and country of incorporation or residence**, which provides users with information about potential foreign jurisdiction restrictions on assets and cash flows.

(b) **ownership / voting interest**, where appropriate, to enable users to understand the nature of the parent's holdings, such as whether they relate to wholly-owned subsidiaries, or if partially-owned, the extent of non-controlling interests.

(c) **main activity**. Consolidation combines subsidiaries with different activities. Disaggregated information relating to activities provides useful information about what individual, material subsidiaries do.

(d) **total assets** as an indication of size, which helps users assess the relative importance of a subsidiary's activities to the group.

12 In practice, a parent has access to information about the subsidiaries it controls and how they fit into the group hierarchy. A listing of material subsidiaries, as opposed to all subsidiaries, would reduce the volume of disclosure required.

13 Materiality is assessed on the significance of subsidiaries to the group, relative to each other. Our assessment is that the number of individually material subsidiaries should be in single figures. Although IFRSs do not provide quantitative guidance on assessing materiality, we think subsidiaries are a form of segmentation. Just as we observe in practice that entities rarely report more than five or six segments, we think that entities should have a similar number of individually material subsidiaries.

Question for the Board

Q1 Do you agree with the proposed disclosure requirements relating to the structure of the group?

Restrictions within the group

Proposed disclosure requirement

14 We propose that a parent be required to disclose the nature of restrictions that are a consequence of assets and liabilities being held by subsidiaries, including:

(a) information about non-controlling interests (NCI) such as:

i its share of the group profit or loss and comprehensive income;

ii its proportionate interest in dividends paid by subsidiaries, distinguishing between dividends paid to the parent and to non-controlling interests; and

iii the extent to which NCI can restrict the activities of subsidiaries, such as restricting cash flows or investment and financial decisions.

(b) legal and contractual restrictions that restrict the ability of subsidiaries to transfer cash to the parent including guarantees between subsidiaries within the group.

(c) the carrying amount of the assets and liabilities to which the restrictions apply.

Staff analysis

15 Paragraph 41 (d) of IAS 27 already requires disclosure of the nature and extent of any significant restrictions (eg resulting from borrowing arrangements or regulatory requirements) on the ability of subsidiaries to transfer funds to the parent in the form of cash dividends or to repay loans or advances.

16 Any restrictions on the ability to move cash within a group affects the availability of cash to the parent. We believe that information on the assets and cash flows that are not fully available to the parent is relevant to users of the financial statements of that parent's group. The disclosure proposals provide more information relating to where within the group cash, assets and debt reside and how cash flows through the group.

Restrictions relating to NCI

17 We propose disclosure requirements relating to NCI, in order to provide information about the profit or loss included in the consolidated financial statements, to which the

parent's shareholders have no claim through the payment of dividends and those consolidated assets and liabilities that the parent cannot access without considering the interests of other owners.

18 The disclosure requirement in paragraph 14 provides users with information about, for example, consolidated assets, which the parent cannot use or access 'entirely as if the assets were its own' because of the legal boundaries that exist within the group (for example, because of protective rights held by NCI that restrict the powers of the parent). It also enables users to identify, for example, the restricted ability of a subsidiary to pay dividends to the parent or repay loans and advances due to the existence of a NCI.

19 The disclosure requirement would also capture information about NCI protective rights that constrain the parent's investing and financing activities, such as veto rights for major capital transactions.

Legal and contractual restrictions

20 In addition to disclosure requirements relating to NCI, we think the disclosure of information about legal and contractual restrictions, including guarantees within the group, would also be relevant to users' needs. For example, a subsidiary may guarantee the debt of another subsidiary and this guarantee may affect the assets and cash flows available to the parent from that subsidiary. Other restrictions may include foreign government restrictions and debt covenants that limit the availability of cash flows to the parent.

21 *Question for the Board*

Q2 Do you agree with the proposed disclosure requirements relating to the nature of restrictions that are a consequence of assets and liabilities being held by subsidiaries?