



Project **Consolidation**

Topic **Disclosures**

Introduction

1. ED10 *Consolidated Financial Statements* (“the ED”) proposes disclosing a reporting entity’s involvement with structured entities that it does not control. The purpose of this paper is to discuss whether and how the proposed disclosures should be amended in the light of respondents’ comments.

Proposed disclosures in the ED

2. The ED describes involvement with a structured entity to include both contractual and non-contractual involvement that exposes the reporting entity to variability of returns.
3. Paragraph B44 of the ED proposes that a reporting entity that has an involvement with an unconsolidated structured entity should disclose among others:
 - (a) the carrying amount of any asset and liability in the reporting entity’s financial statements that might have arisen from its involvement with - the unconsolidated structured entity (eg. a guarantee);
 - (b) the reported amount of the assets in the financial statements of the structured entity; and
 - (c) the amount that best represents the reporting entity’s maximum exposure to loss from its involvement with the structured entity, including how the maximum exposure to loss is determined.

This paper has been prepared for discussion at a public meeting of the Analyst Representative Group and Global Preparers Forum of the IASB.

The views expressed in this paper are those of the authors.

Comments made in relation to the application of an IFRS do not purport to be acceptable or unacceptable application of that IFRS—only the IFRIC or the IASB can make such a determination.

The tentative decisions made by the IASB at its public meetings are reported in IASB *Update*. Official pronouncements of the IASB, including Discussion Papers, Exposure Drafts, IFRSs and Interpretations are published only after it has completed its full due process, including appropriate public consultation and formal voting procedures.

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4. In addition, paragraph B41 of the ED proposes that a reporting entity discloses:
 - (a) income from its involvement with structured entities that it has set-up or sponsored; and
 - (b) the value of assets transferred to those structured entities, at the date the transfers were made.

Respondents' comments

Principle

5. Most users agreed with the proposed disclosures because they thought that to obtain a better understanding of the risks associated with a reporting entity's involvement with unconsolidated structured entities a user would need information about the activities, the assets and, if relevant, liabilities of the structured entity that affect the reporting entity's risk exposure as well as the reporting entity's maximum loss exposure.
6. In contrast, most preparers disagreed with the proposed disclosures and argued that the counterparty should not matter for the analysis of the reporting entity's risk exposure. Preparers believed that a risk analysis should focus on the instruments that create risk, regardless of whether the risk is associated with a reporting entity's involvement with a structured entity or a traditional entity. They believe that instead of expanding the disclosure requirements in the consolidation standard, the Board should focus on improving the requirements in IFRS 7 *Financial Instruments: Disclosures*.

Question 1

When assessing a reporting entity's off-balance sheet risks, which information would be more useful: Information about the reporting entity's exposure to risks from financial instruments? Or, information about the reporting entity's risk exposure to particular counterparties (eg. structured entities)? Would you require disclosures about the counterparties, even though IFRS 7 already requires disclosures about the risk exposure from financial instruments? Why?

Scope

7. Most users believed that the analysis of a reporting entity's risk exposure from its involvement with unconsolidated structured entities is of particular practical relevance. However, some users asked the Board to extend the scope of the proposed disclosure requirements because:
- (a) as indicated above, risks arise independent of the legal structure of the counterparty. Therefore, they would extend the scope of the disclosures to all entities, regardless of whether they are structured entities or traditional entities. They note also that such a disclosure would avoid the need to define a structured entity in the final standard.
 - (b) risks arise from unconsolidated and consolidated (structured) entities. Therefore, some users argue that a reporting entity should also disclose its risk exposure from consolidated entities.
8. Most preparers asked the Board to limit the scope of the proposed disclosures. They noted that the term "involvement" has a wide meaning and captures any relationship with a structured entity, including arm's length service provider relationships. Preparers questioned the need to disclose minor risk exposures from ordinary business transactions. Therefore, they argued that the proposed requirements should apply only to "significant" involvements.

Question 2

Should the reporting entity disclose risks from its involvement with:

- (a) unconsolidated structured entities;
- (b) unconsolidated and consolidated structured entities;
- (c) all unconsolidated entities; or
- (d) all unconsolidated and consolidated entities?

Would you require the disclosures for any risk exposure or for significant risk exposures only? Why?

Information provided

9. Most preparers were concerned that the extent of data to be generated for those entities that are within the scope of the disclosures had the potential to hide rather than disclose the key messages about a reporting entity's risk exposure. They argued also that it would often be difficult to obtain information about the assets and liabilities of an entity that it does not control, particularly if the entity has a different reporting date or does not prepare IFRS-financial statements.
10. In addition, preparers believed that disclosing the value of assets transferred to structured entities that the reporting entity has set-up or sponsored, but does not have any ongoing involvement in, provides little assistance in assessing the risk exposure of the reporting entity. Therefore, they would remove the disclosure in paragraph B41 of the ED.
11. Users believed that most of the proposed disclosures, including those about structured entities that the reporting entity has set-up or sponsored, were important for their assessment of the reporting entity's risk exposure and should be carried over into the final standard. They referred to the experience in the U.S. where preparers had already to apply similar disclosures. In their view, U.S.-preparers were able to generate the necessary data and to present it in an understandable format.

Question 3

How can the final standard ensure that a reporting entity discloses only relevant information? Should the standard provide only broad disclosure objectives and leave it open how those objectives could best be met? Or, should the standard prescribe detailed disclosures and formats to ensure that particular information will always be provided?

How useful are the proposed disclosure requirements in paragraphs B38-B47 of the ED? Which disclosures could be deleted? Are important disclosures missing?