



Staff Paper

Project	Consolidation
Topic	Disclosures – Sweep issues

Introduction

1. Agenda paper 3A identifies a set of disclosure objectives. At their joint meeting in April 2010 the boards tentatively decided that those disclosure objectives should be supplemented by specific disclosure requirements. The boards have also come to tentative conclusions for some specific disclosure requirements.
2. This agenda paper discusses the specific remaining disclosure requirements for which the boards have not yet concluded. The disclosure requirements are presented as follows:
 - (a) a reporting entity's basis of control;
 - (b) the interest that the non-controlling interests have in the group's activities;
 - (c) a reporting entity's risk exposure to:
 - (i) consolidated structured entities;
 - (ii) unconsolidated structured entities with which the reporting entity is involved;
 - (iii) unconsolidated structured entities that the reporting entity has set up or sponsored, but with which it does not have any continuing involvement.

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Basis of control

3. Agenda paper 3A recommends that a reporting entity should provide information that helps users to understand the significant judgements and assumptions (and changes to those judgements and assumptions) made by the reporting entity in determining whether it controls (or does not control) another entity and/or the reporting entity's involvement with a structured entity.
4. Some staff believe that in order to meet this disclosure objective, there should be a specific disclosure requirement focusing on situations when an interest holder has a significant investment in an entity, but concludes that it does not have the power to direct the activities of the other entity. Those staff believe that, in this case, the reporting entity should disclose the surrounding facts and circumstances that underlie the basis for its consolidation conclusion and the rationale or strategy for holding a significant investment in an entity without obtaining control of the entity.
5. Other staff do not believe that this specific disclosure is necessary. Those staff note that a reporting entity's conclusion that it does not control another entity, even though it holds a significant investment in that entity, would generally require significant judgement. Therefore, the disclosure objective in paragraph 3 would already require the reporting entity to disclose information about its decision not to consolidate that entity.
6. Those staff do not believe that the final disclosure requirements should identify specific scenarios, in which a reporting entity must disclose information about its basis of control. Rather, a reporting entity should disclose all significant judgements and assumptions made in determining whether a reporting entity should consolidate another entity, or not. Furthermore, they do not believe that the rationale or strategy for holding a significant investment should be discussed in the disclosures relating to the reporting entity's basis of control. In their view, the reporting entity's rationale or strategy for holding particular investments should be discussed in management commentary.

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Question 1 for the boards

(1) When a reporting entity has a significant investment in an entity but concludes that it does not have the power to direct the activities of the other entity, do the boards believe that a reporting entity should be required to specifically disclose:

(a) the surrounding facts and circumstances that underlie the basis for its conclusion; and

(b) the rationale or strategy for holding a significant investment in an entity without obtaining control of the entity, including any strategies employed to mitigate the risks from that investment.

The interest that the non-controlling interests have in the group's activities

7. Agenda paper 3A recommends that a reporting entity should provide information that helps users to understand the interest that the non-controlling interests have in the group's activities. Some staff believe that, in order to meet the disclosure objective, a reporting entity should provide the following disclosures **for subsidiaries that have non-controlling interests that are individually material to the reporting entity**:
- (a) **the name** because naming subsidiaries that have non-controlling interests that are individually material to the reporting entity helps users to search for other information that might be useful for their analysis of the subsidiary.
 - (b) **the country of incorporation or residence** because this assists users in understanding the political, economic and currency risk associated with those subsidiaries.
 - (c) **the proportion of ownership interest and, if different, proportion of voting rights held** because this information enables users to understand the earnings/cash flows attributable to the shareholders of the parent and the amount attributable to non-controlling interests.
 - (d) **summarised financial information for the subsidiary**, such as the subsidiary's assets, liabilities, revenues, profit or loss, dividends paid to

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non-controlling interests and cash flows (before intercompany eliminations). Again, this information would help users to understand the earnings/cash flows attributable to the shareholders of the parent and the amount attributable to non-controlling interests.

8. Those staff do not believe that the proposed disclosures would impose excessive costs on preparers of financial statements because the information to be disclosed would generally be available to the reporting entity when preparing consolidated financial statements.¹ In addition, they emphasise that the proposed disclosures would be limited only to subsidiaries that have non-controlling interests that are individually material to the reporting entity, rather than all subsidiaries of the reporting entity.
9. Other staff do not believe that the disclosures proposed in paragraph 7 of this paper should be required as part of this project. They believe that the objective of providing such disclosures would be similar to the objectives of providing segment information. They believe that if the boards think that segment information does not enable users to evaluate the nature and financial effects of a particular business activity, the boards should examine whether the requirements for segment reporting need to be revised as part of a separate project.
10. Additionally, those staff believe that the legal structure is often irrelevant. For example, a reporting entity with manufacturing operations may establish a number of legal entities in different states or countries to perform product distribution in order to minimize their tax expense. Alternatively, a reporting entity may have a central finance entity that manages finances for the consolidated group and all of the intercompany loans held by the finance entity

¹ There might be situations, in which a subsidiary neither prepares financial statements in accordance with IFRSs nor does the reporting entity prepare a reconciliation of the subsidiary's financial statements to IFRSs, because it prepares the group financial statements directly without recourse to the individual financial statements of its subsidiaries. We acknowledge that, in those cases, the proposed disclosure requirement would impose additional costs on the reporting entity. However, we note that paragraph 37(b) of IAS 28 *Investments in Associates* contains a similar disclosure requirement for the reporting entity's investments in associates. We are not aware that this disclosure requirement has imposed insurmountable challenges on preparers.

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are eliminated on consolidation. These staff believe that including information about these entities' separate financial statements is not relevant to users and would complicate the financial statements.

Question 2 for the boards

(2) For subsidiaries with non-controlling interests that are individually material to the reporting entity, do the boards believe that the reporting entity should disclose:

- (a) the name;
- (b) the country of incorporation or residence;
- (c) the proportion of ownership interest and, if different, proportion of voting interest held; and
- (d) summarised financial information?

Risk disclosures for consolidated structured entities

11. Paragraph 810-10-50-3(d) requires that the reporting entity should disclose the terms of arrangements that could require the reporting entity to provide financial support (for example, liquidity arrangements and obligations to purchase assets) to consolidated structured entities, including events or circumstances that could expose the reporting entity to a loss.
12. Some staff recommend that this disclosure requirement be included in the final disclosure requirements because they believe that the disclosure requirement is consistent with the disclosure objective, according to which a reporting entity should provide information that helps users to understand the nature of, and changes in, the risks associated with the reporting entity's control of structured entities.
13. At the joint meeting in April 2010, some board members agreed with the proposed disclosure requirement, but questioned, why the requirement should be limited to structured entities only. Those board members argued that risks could arise from all consolidated entities, irrespective of whether the entity is considered a structured entity and that, therefore, the proposed disclosures should apply to all entities.

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14. The staff acknowledges that it would help users in their understanding of the risk exposure of the reporting entity if the reporting entity provided the disclosure discussed in paragraph 11 for all subsidiaries.
15. However, some staff propose to restrict those disclosures to consolidated structured entities. In their view, it is not the goal of the consolidation project to conduct a comprehensive review of the disclosures for a reporting entity's general risk exposure. Rather, this project focuses on targeted improvements to a reporting entity's risk disclosures relating to its involvement with consolidated and unconsolidated structured entities. Those improvements are a direct response to concerns raised in the wake of the credit crises about the lack of disclosures for structured entities. Those staff recommend that the boards do not extend the scope of the consolidation project, but discuss risk disclosures for entities, other than structured entities, as part of a more comprehensive review of the boards' disclosure framework.
16. In addition, those staff believe that it would be difficult to make the recommendation operational for all entities as this would require detailed information about all commitments (including loans) between a parent and any of its subsidiaries.
17. Other staff agree that it would be difficult to make the recommendation operational for all entities as part of this project. However, they also agree with those board members who argue that risks could arise from all consolidated entities, irrespective of whether the entity is considered a structured entity. Those staff do not see a reason to require particular disclosure requirements only for some consolidated entities, and not others. Therefore, they recommend that the proposed disclosure requirement not be included in the final disclosure requirements. Rather, they would recommend that risk disclosures for all consolidated entities are discussed as part of a more comprehensive review of the disclosure framework.

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Question 3 for the boards

(3) Do the boards believe that a reporting entity should disclose the terms of an arrangement that could require the reporting entity to provide financial support (for example, liquidity arrangements and obligations to purchase assets) to a consolidated structured entity, including events or circumstances that could expose the reporting entity to a loss?

Risk disclosures for unconsolidated structured entities with which the reporting entity has an involvement

18. Agenda paper 3A recommends that a reporting entity should disclose the nature of, and changes in, the risks associated with the reporting entity's involvement with unconsolidated structured entities. We believe that in order to meet this disclosure objective a reporting entity should be required to specifically disclose:
- (a) the carrying amount of the assets and liabilities recognised in the reporting entity's consolidated financial statements relating to the reporting entity's involvement with unconsolidated structured entities;
 - (b) the line items in the consolidated statement of financial position in which those assets and liabilities are recognised;
 - (c) the amount that best represents the reporting entity's maximum exposure to loss from its involvement with unconsolidated structured entities, including how the maximum exposure to loss is determined. If a reporting entity cannot quantify its maximum exposure to loss from its involvement with unconsolidated structured entities it must disclose that fact;
 - (d) a comparison of the carrying amount of the assets and liabilities of the reporting entity that relate to the reporting entity's involvement with unconsolidated structured entities and the reporting entity's maximum exposure to loss.

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19. The staff recommendation is consistent with the disclosure requirements in paragraph 810-10-50-4. ED 10 proposed a similar disclosure, but:
 - (a) required a reporting entity to also disclose the reported amount of assets held by structured entities with which the reporting entity has an involvement, measured at the date of the reporting entity's consolidated financial statements and the measurement basis of the reported amounts; and
 - (b) did not require a reporting entity to disclose a comparison of the carrying amount of the assets and liabilities of the reporting entity that relate to the reporting entity's involvement with unconsolidated structured entities and the reporting entity's maximum exposure to loss.
20. We no longer believe that a separate requirement to disclose the assets held by a structured entity and their measurement basis is necessary. The boards have decided at their joint March 2010 meeting that a reporting entity should disclose the nature, purpose, size and activities of an unconsolidated structured entity and how the structured entity is financed. In our view, this requirement would normally include information about the assets held by the structured entity and the funding of those assets.
21. We recommend that the boards require a reporting entity to disclose a comparison of the carrying amount of the assets and liabilities of the reporting entity that relate to the reporting entity's involvement with unconsolidated structured entities and the reporting entity's maximum exposure to loss. We believe that such a comparison will provide users with a better understanding of the differences between the reporting entity's maximum loss exposure and the reporting entity's expectation as to whether it is likely that it will bear all or only some of those losses.

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Question 4 for the boards

- (4) Do the boards agree that a reporting entity should disclose:
- (a) the carrying amount of the assets and liabilities recognised in the reporting entity's consolidated financial statements relating to the reporting entity's involvement with unconsolidated structured entities;
 - (b) the line items in the consolidated statement of financial position in which those assets and liabilities are recognised;
 - (c) the amount that best represents the reporting entity's maximum exposure to loss from its involvement with unconsolidated structured entities, including how the maximum exposure to loss is determined. If a reporting entity cannot quantify its maximum exposure to loss from its involvement with unconsolidated structured entities it must disclose that fact; and
 - (d) a comparison of the carrying amount of the assets and liabilities of the reporting entity that relate to the reporting entity's involvement with unconsolidated structured entities and the reporting entity's maximum exposure to loss? If not, why?

Risk disclosures for unconsolidated structured entities that the reporting entity has set up or sponsored

22. When a reporting entity has no continuing involvement with a structured entity there is no financial instrument or existing relationship as an anchor for assessing risk. However, setting up or sponsoring a structured entity can create risks for the sponsoring entity, particularly when the sponsoring entity selects the assets or marketed the vehicle to prospective investors to invest in the vehicle. If the structured entity encounters difficulties it is possible that the sponsor could be challenged on their advice or actions (ie were they negligent, did they provide adequate advice to investors etc) or may choose to act to protect its reputation.
23. Therefore, paragraph B41 of ED 10 proposed that, for unconsolidated structured entities that the reporting entity has set up or sponsored, the reporting entity disclose a summary of:

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- (a) income from the reporting entity's involvement with structured entities, including a description of the types of income presented in the summary; and
- (b) the value of assets transferred to those structured entities, at the date the transfers were made.

These requirements would be required for all unconsolidated structured entities that the reporting entity has set up or sponsored, including those structured entities whose assets were acquired from a third party. The disclosure requirements would apply, regardless of whether there is a continuing involvement with the structured entity.

24. The proposed disclosures were designed to give users of financial statements a sense of the scale of the operations the reporting entity had managed with these types of transactions. The proposals were not intended to help assess the actual risk of failure or recourse (including as a result of negligence) to the reporting entity but they would give a sense of the scale involved and the extent of the reporting entity's reliance on such entities to facilitate its business. For example, as the credit crisis developed investors became concerned about the extent that banks had been involved with structured investment vehicles (SIVs). However, few banks reported information about the extent of their involvement with establishing SIVs. It was, therefore, difficult to assess the potential exposure a particular entity might have to such vehicles.
25. The proposals required that income is used as the disclosure anchor because, in many cases, there would be no asset or liability associated with sponsored vehicles on the reporting entity's statement of financial position. The income disclosures were therefore not intended to convey information in their own right, but the intention was that they would be the anchor on which the asset disclosures would be based.²

² The revenue earned relative to the assets managed or sponsored might convey information about the relative involvement the reporting entity had with the vehicle (ie the larger the percentage fee or commission the greater the involvement), but that was an ancillary benefit.

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26. Our discussions with users have confirmed that they believe that it would be very useful to have information about the scale of a reporting entity's operations that is derived from transactions with unconsolidated structured entities, ie to have more information about a reporting entity's business model and the risks associated with that business model. This would be particularly useful if a reporting entity were no longer able to generate fee income from its involvement with structured entities because of particular events that might cause a significant decrease in the use of such entities for investing or financing purposes. Those users also confirmed that their request for such information precedes the financial crisis, and is not simply a reaction to it.
27. Some staff believe that reporting entities face many risks from their past activities and such business risks should be addressed more generally, perhaps in Management Commentary. Therefore, those staff would argue that the proposed disclosure requirement, if considered necessary, should *not* be part of a disclosure package that addresses a reporting entity's exposure to risk from its involvement with unconsolidated structured entities.
28. In addition, those staff believe that the disclosures about the nature and extent of a reporting entity's involvement with unconsolidated structured entities already agreed to by the boards are sufficient (ie, to require a reporting entity to disclose qualitative and quantitative information about its involvement with unconsolidated structured entities, including information about the nature, purpose, and activities of structured entities, including how those activities are financed). They believe that if a reporting entity does not have any continuing involvement with a structured entity then including this requirement would contradict the disclosure objective, according to which a reporting entity should disclose the nature of, and changes in, the risks associated with the reporting entity's **involvement** with unconsolidated structured entities.
29. Other staff see the structured entity disclosures that the boards confirmed at the March meeting as a direct response to concerns related to investment and securitisation activities in the wake of the financial crisis and the observation that the risks associated with some activities are more systemic than others.

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Therefore, in order to address the requests for such information from users, those staff recommend that the disclosures proposed in paragraph B41 of ED 10 are retained in the final standard.

30. Appendix A to this agenda paper addresses further application issues if the boards should decide to retain the proposed disclosure.

Question 6 for the boards

- (6) Do the boards believe that a reporting entity should be required to disclose:
- (a) income from its involvement with unconsolidated structured entities that it has sponsored; and
 - (b) the carrying amount of assets held by those structured entities at the time that the structured entities are established?

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Appendix A: Further application issues relating to the disclosure proposed in paragraph B41 of ED 10

1. Most respondents to ED 10 recommended that the IASB should remove the proposed disclosure requirement. However, if the boards should affirm the proposed disclosure requirements, respondents requested application guidance as to the following:
 - (a) When has a reporting entity sponsored or set up a structured entity and is there a difference between those terms? For example, do the disclosure requirements apply when the reporting entity has provided technical services as an agent of other parties only? Respondents generally acknowledged that the terms “sponsor” and “set up” are used in the disclosures of many reporting entities. However, in their view, those terms are used with more than one meaning. Therefore, they were concerned that, if those terms are not defined, divergence in practice might arise.
 - (b) What represents income from a reporting entity’s involvement with a structured entity? Does the requirement mean fee income only or did it intend a reporting entity to disclose all cash flows generated by its involvement with an unconsolidated structured entity? Some respondents also thought that the requirement should be to disclose cash flow information, rather than income information.
 - (c) To which transfers should the disclosure requirement apply? Would transfers at fair value be included in the disclosure? Also, does the disclosure requirement apply to transfers of the current period only or is it intended to be cumulative? In addition, some respondents questioned whether a reporting entity should also disclose transfers from the structured entity to the reporting entity.
 - (d) How should the “value” of assets transferred to a structured entity be measured? How should a reporting entity aggregate the required information if it has transferred assets at different dates and for

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different values? Some respondents thought that a more practical disclosure was to require a reporting entity to disclose the carrying amounts of assets transferred to a structured entity at the reporting date, rather than at the date of the transfer.

2. In response to respondents' requests for clarification of the disclosure proposals in paragraph B41, the staff supporting the inclusion of the disclosure proposals in B41 recommend the following:

Set up or sponsored

3. The disclosure should continue to be required for unconsolidated structured entities that the reporting entity has sponsored. Many respondents argued that without being defined, that term could be interpreted differently. Although we acknowledge that this could be the case, the term is already widely used in practice. We recommend two changes to further mitigate interpretation difficulties relating to those terms:
 - (a) Rather than using two undefined terms, the final standard should only refer to structured entities that the reporting entity has sponsored, but not include separately the term 'set up';
 - (b) The final standard should require a reporting entity to explain how it has interpreted 'sponsored' when providing the required disclosures.

Income from a reporting entity's involvement with unconsolidated structured entities

4. The staff recommend that the term 'income' should be defined to include not only fee income from sponsoring the structured entity, but also fee income from continuing to provide services, gains or losses if the reporting entity sold assets to the structured entity, and interest income or fair value gains or losses from any equity or debt securities that the reporting entity might hold in the structured entity.

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The value of assets transferred to the structured entities at the date the transfers were made

5. We recommend that the final standard require a reporting entity to disclose the UUUcarrying amount of assets held by the structured entities at the time that the structured entities are established for the following reasons:
 - (a) The objective of the disclosure of assets is to provide a sense of the scale of the structured entities' operations that the reporting entity has been involved with. This might imply that the disclosures should require the cumulative amount of assets recognised by those structured entities, or possibly, for the value of the assets of the structured entities at the end of the reporting period. However the staff do not believe that asking for the cumulative amount of assets recognised by the structured entities would provide useful information—often, asset purchases of structured entities are simply to replace assets that have been paid by the counterparties to those assets (eg revolving short-term receivable securitisations such as credit card or trade receivable securitisations), or to replace assets that have been sold (eg investment vehicles).
 - (b) The staff propose that a reporting entity should disclose the carrying amount of the assets recognised by the structured entities at the time that the structured entities are established. We believe that the reporting entity should have information about the carrying amount of the assets recognised by the structured entity at that time assuming that it has sponsored the structured entity.
6. The staff do not recommend retaining the requirement in paragraph B42 of ED 10 to provide the information for the current reporting period and the preceding two reporting periods. We agree with those respondents that questioned why this disclosure would be required for a specified minimum period that is different from the general requirements for comparatives, which apply to all of the other disclosure requirements relating to a reporting entity's involvement with structured entities.