



| | |
|---------|---|
| Project | Consolidation |
| Topic | Investment companies—first-time adoption in 2011 |

Introduction and staff analysis

1. Several jurisdictions will require entities to prepare their financial statements in accordance with IFRSs for the first time from 1 January 2011. Some of those jurisdictions have existing requirements for the type of entity we are calling an *investment company* that require them to measure investments in entities they control at fair value, rather than consolidating those investments.
2. In February, the Board tentatively decided that an investment company would be required to measure investments in entities that it controls at fair value through profit or loss. That tentative decision has been welcomed by those jurisdictions.
3. We expect to publish the investment company exposure draft for comment in June 2010. We are recommending a 90-day comment period for that exposure draft. On this basis, the earliest that the investment company issue could be finalised would be October/November 2010 (and that assumes that we ‘fast-track’ and finalise the investment company proposals before the remainder of the final consolidation standard).
4. We are told that this timing creates a dilemma for, potentially, affected entities. If the entities assume that the Board will finalise the fair value measurement proposals by investment companies before the end of 2010, and not prepare for consolidation, they might not be in a position to prepare IFRS financial statements as from 1 January 2010 if the Board decides *not* to finalise, or to change the scope of, the proposals. On the other hand, entities might assume that the Board will *not* finalise the fair value measurement proposals before the

This paper has been prepared by the technical staff of the IASCF for discussion at a public meeting of the IASB.

The views expressed in this paper are those of the staff preparing the paper. They do not purport to represent the views of any individual members of the IASB.

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.

IASB Staff paper

end of 2010, and incur significant costs in preparing to consolidate controlled investees only to see the proposals finalised before the end of the year.

5. The standard-setters and regulators in some of those territories want to avoid those entities having to undertake two significant accounting changes within a short timeframe—firstly, to change from fair value accounting to consolidation of controlled investees, perhaps for as little as one or two reporting quarters; then, to change back to fair value accounting from consolidation.
6. Those standard-setters and regulators would prefer not to address this matter themselves because any jurisdiction-specific solution has the potential to create other unforeseen issues when adopting IFRS. We have been asked if the Board would consider addressing the issue through an amendment to IFRS 1.
7. They have suggested that the Board amend IFRS 1 *First-time Adoption of International Financial Reporting Standards* as follows:

to permit a first-time adopter of IFRS to continue to apply its previous accounting for investments in entities that it controls (rather than IAS 27) for a limited period until the final consolidation standard is published if:

- (a) it measures investments in entities that it controls at fair value according to its previous accounting requirements; and
- (b) it would meet the definition of an investment company according to the IASB investment company exposure draft published in Q2 2010.¹

The amendment in IFRS 1 would expire as soon as the final consolidation standard would be published. If the Board decided not to publish a new consolidation standard, the amendment in IFRS 1 would be removed as soon as the Board would make that decision.

8. Some staff believe that this the best way to address the issue for the following reasons:

¹ The amendment to IFRS 1 would need to replicate the criteria and application guidance that defines an investment company included in the investment company exposure draft because it could not refer to a document that is not part of IFRS literature.

IASB Staff paper

- (a) the amendment would permit those that already measure investments in entities that they control at fair value (and are expected to be required to do so according to the new consolidation standard) to continue to measure those investments at fair value until the consolidated standard is finalised. This is similar to the approach taken in IFRS 4 *Insurance Contracts* and IFRS 6 [title] that permits some entities to continue to use their previous accounting requirements until standards are finalised that specifically address the nature of their activities.
 - (b) the issue affects first-time adopters of IFRS only. Therefore, including the amendment within IFRS 1 narrows its application to first-time adopters, and only to those first-time adopters that already measure investments in entities that they control at fair value. [An amendment, for example, to IAS 27 would apply to all IFRS-preparers.]
 - (c) amending IFRS 1 avoids putting time pressure on the IASB's due process that might be the case if the Board were to decide to 'fast track' completing the investment company proposals either as part of finalising the consolidation standard or before finalising the remainder of the consolidation standard.
9. Other staff think this approach is inappropriate because:
- (a) It relies on inserting into IFRS 1 a definition of an investment company by reference to a definition in an exposure draft.
 - (b) Such an amendment would lead to entities asserting compliance with IFRSs on the basis of their local GAAP. If the Board ultimately decides that the investment company approach is not appropriate, or it amends the definition of an investment company, some or all of the entities taking advantage of the concession will have to consolidate their investments. Those entities will have been asserting compliance with IFRS by accounting for such investments in a manner currently not permitted by IFRSs and possibly never permitted by IFRSs. IFRS 1 is designed to help entities transition into the current IFRS requirements and not possible future requirements. It is not like insurance

IASB Staff paper

accounting or extractive activities where there were no specific IFRS requirements. IAS 27 addresses investment companies clearly and explicitly—there are current requirements.

- (c) The affected jurisdictions are likely to have the ability to defer application of IFRSs to investment companies if they are concerned about this matter.

- 10. If the Board decides to amend IFRS 1, we would recommend incorporating this proposed amendment with a number of other IFRS 1 issues that the IFRIC are addressing in May—hard-wired dates in IFRS 1, and clarification of the borrowing costs exemption for projects in progress. The proposed amendment could be published in June 2010.

Questions for the Board

- (1) Does the Board wish to address this issue that affects some first-time adopters of IFRSs in 2011?
- (2) If yes, do you agree that this should be done as an amendment to IFRS 1 as proposed in paragraph 7 of this paper?