

STAFF PAPER

12-13 November 2013

IFRS Interpretations Committee Meeting

Project	IFRS 10 <i>Consolidated Financial Statements</i>
Paper topic	Investment Entities Amendments—The interaction between the investment entity amendments and the exemption from preparing consolidated financial statements requirements in IFRS 10
CONTACT(S)	Koichiro Kuramochi kkuramochi@ifrs.org +44 (0)20 7246 6496

This paper has been prepared by the staff of the IFRS Foundation for discussion at a public meeting of the IFRS Interpretations Committee. Comments made in relation to the application of an IFRS do not purport to be acceptable or unacceptable application of that IFRS—only the IFRS Interpretations Committee or the IASB can make such a determination. Decisions made by the IFRS Interpretations Committee are reported in *IFRIC Update*. The approval of a final Interpretation by the Board is reported in *IASB Update*.

Introduction

1. In July 2013, the IFRS Interpretations Committee (‘the Interpretations Committee’) received a request to clarify some issues related to the Investment Entities amendments to IFRS 10, IFRS 12 and IAS 27. One of the issues relates to the interaction between the investment entity amendments and the exemption from preparing consolidated financial statements requirements in IFRS 10.
2. IFRS 10 requires a parent entity to present consolidated financial statements. However, IFRS 10 paragraph 4 provides relief whereby a parent need not present consolidated financial statements if it meets particular conditions, including the requirement that “its ultimate or any intermediate parent produces consolidated financial statements that are available for public use and comply with IFRSs.”
3. There are two issues to be addressed. The first issue is whether the exemption is applicable if its ultimate or any intermediate parent is an investment entity which prepares consolidated financial statements but measures investees at fair value (as described in paragraph 6 of this Agenda paper). The second issue is whether the intermediate parent loses the exemption if the ultimate parent does not present

consolidated financial statements. This would be the case if the parent entity prepares one set of financial statements in which it accounts for all of the investments at fair value, because it does not have a subsidiary which provides investment-related services (as in paragraph 16 of this Agenda paper).

Paper structure

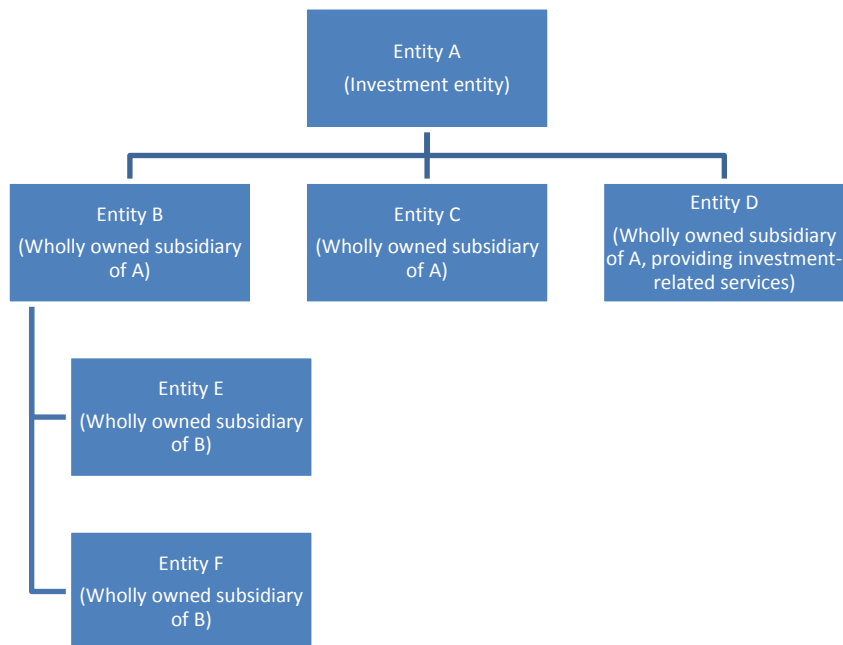
4. This paper is organised as follows:
 - (a) Submission received;
 - (b) Extract from the Standards;
 - (c) Staff analysis of the issue;
 - (d) Summary of outreach conducted;
 - (e) Assessment against the interpretations agenda criteria; and
 - (f) Staff recommendation.

Submission received

5. IFRS 10 requires an entity that is a parent to present consolidated financial statements. However, IFRS 10 paragraph 4(a) states that a parent need not present consolidated financial statements if it meets certain conditions, including the condition in paragraph 4(a)(iv) that its ultimate or any intermediate parent must produce consolidated financial statements that are available for public use and comply with IFRSs. The Investment Entities amendments did not change the requirements in IFRS 10 paragraph 4(a).
6. The submitter claims that this raises a question as to the application of the exemption in IFRS 10 paragraph 4(a) to the subsidiary of an investment entity, when that subsidiary is itself a parent. Specifically, the question asked is whether the requirement in IFRS 10 paragraph 4(a)(iv) met only when the results of the entity have been included by way of consolidation in the parent or intermediate parent consolidated accounts? Can it also be met if the entity has been reflected at fair value in the consolidated accounts of the parent or intermediate parent?

7. The submitter presented the following example:

Entity A meets the definition of an investment entity in accordance with IFRS 10 (as amended). Entities B, C and D are all wholly owned subsidiaries of Entity A and Entity E and F are wholly owned subsidiaries of Entity B. Entity D is an entity that provides services that relate to the investment activities of Entity A and that is consolidated by Entity A under IFRS 10 paragraph 32. Consequently, Entity A produces consolidated financial statements that consolidate Entity D and reflect the investments in Entities B and C at fair value.



Assuming all other conditions in IFRS 10 paragraph 4 (as amended) are met, the question is whether Entity B can apply the exemption from presenting consolidated financial statements under IFRS 10 paragraph 4(a) as a result of Entity A producing consolidated financial statements.

8. The submitter notes that there are two alternative views in practice.

- (a) **View A: No. The intention of IFRS 10 paragraph 4 is that Entity B should produce consolidated financial statements, because its consolidated financial information is not included in the consolidated financial statements of Entity A.**

- (b) **View B: Yes. Because Entity A produces consolidated financial statements, Entity B can apply the exemption from presenting consolidated financial statements, regardless of whether Entity B itself is accounted for under the consolidation method in those financial statements.**

Extract from the Standards

9. A parent need not present consolidated financial statements if it meets particular conditions, including the condition that its ultimate or any intermediate parent produces consolidated financial statements that are available for public use and comply with IFRSs, in accordance with paragraph 4(a) (iv) of IFRS 10.

4 An entity that is a parent shall present consolidated financial statements. This IFRS applies to all entities, except as follows:

(a) a parent need not present consolidated financial statements if it meets all the following conditions:

(iv) its ultimate or any intermediate parent produces consolidated financial statements that are available for public use and comply with IFRSs.

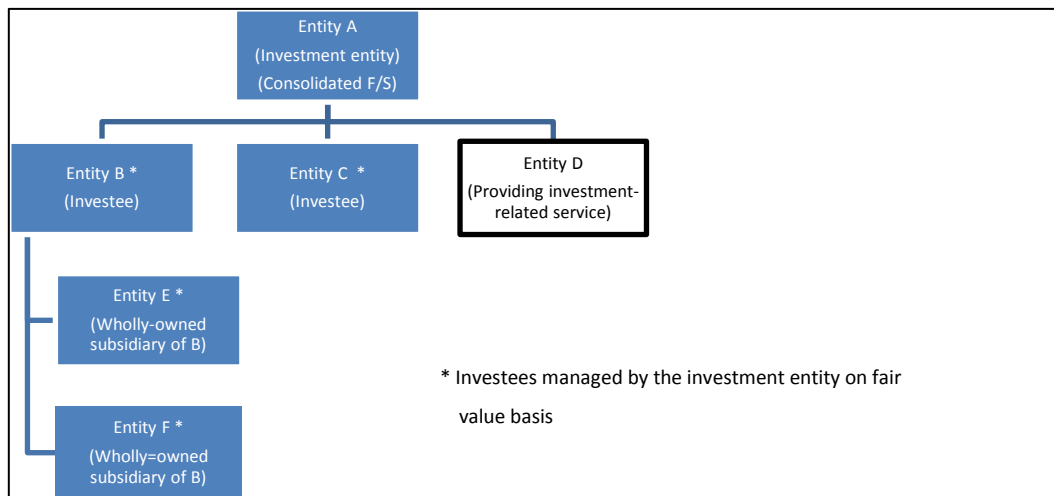
10. If a subsidiary provides services that relate to the investment entity's investment activities, the investment entity shall consolidate the subsidiary, in accordance with paragraph 32 of IFRS 10.

32 Notwithstanding the requirement in paragraph 31, if an investment entity has a subsidiary that provides services that relate to the investment entity's investment activities (see paragraphs B85C–B85E), it shall consolidate that subsidiary in accordance with paragraphs 19–26 of this IFRS and apply the requirements of IFRS 3 to the acquisition of any such subsidiary.

Staff analysis of the issue

Case 1: Analysis on the example on the submission

11. In the example in the submission, Entity D, which is a subsidiary of the ultimate parent, provides investment-related services. Accordingly, Entity A, the ultimate parent, is required to prepare consolidated financial statements, in accordance with paragraph 4. The question raised is: can Entity B apply the exemption from presenting consolidated financial statements, in accordance with paragraph 4(a) (iv) of IFRS 10?



12. In the submission, two views are presented as follows:
- View A: Entity B should produce consolidated financial statements, because its consolidated financial information is not included in the consolidated financial statements of Entity A.
 - View B: Entity B can apply the exemption from presenting consolidated financial statements because Entity A produces consolidated financial statements, regardless of whether Entity B itself is accounted for under the consolidation method in those financial statements.
13. We support View B because paragraph 4(a) (iv) of IFRS 10 does not specify how the results of subsidiaries should be presented in the consolidated financial statements. Accordingly, we think that paragraph 4(a) (iv) of IFRS 10 also applies when the intermediate parent has been accounted for at fair value through

profit or loss in the consolidated financial statements in accordance with paragraph 31 of IFRS 10.

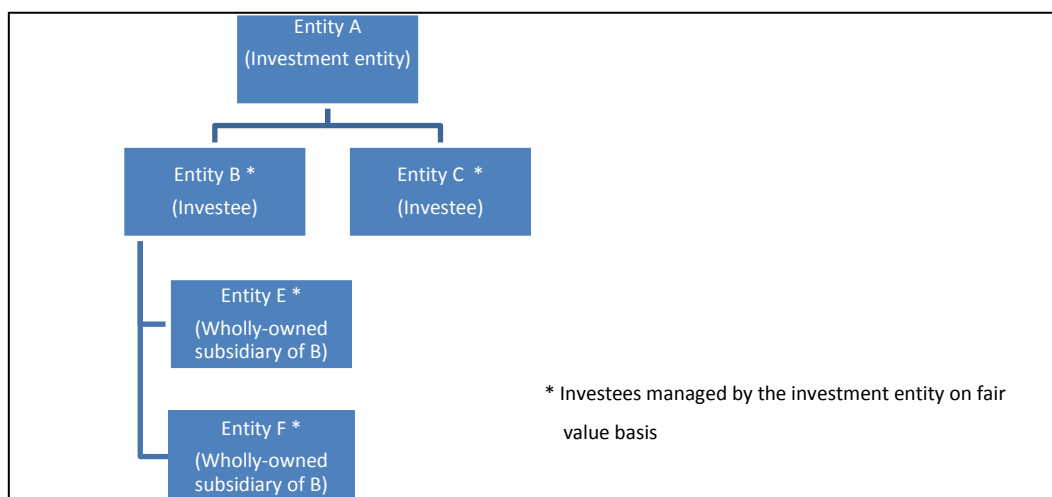
14. We do not support View A. We do not think that the Investment Entity amendments have disrupted the exemption in this case. Paragraph 4(a)(iv) only requires the higher parent to produce consolidated financial statements and it does not specify how the intermediate parent needs to be incorporated into those consolidated financial statements.
15. In this case, Entity A, the ultimate parent, is an investment entity. Accordingly, we do not think Entity B is required to separately produce consolidated financial statements as View A suggests.

Case 2: Analysis of the case if its ultimate or any intermediate parent does not produce consolidated financial statements

16. We noted that, in the submission, View B has an additional paragraph as follows (emphasis added):

However, **if entity D did not exist, the answer would change under this view.** This is because Entity A would not be preparing consolidated financial statements if it only held investments in Entity B and Entity C. That is, both investments would be measured at fair value through profit or loss under IFRS 10.31. IAS 27.8A emphasises that if a parent is required to measure all of its subsidiaries at fair value through profit or loss in accordance with IFRS 10.31, the parent entity presents separate financial statements as its only financial statements. **Because Entity A (the ultimate parent) would not prepare consolidated financial statements, Entity B fails to meet the condition in IFRS 10.4(a)(iv) and accordingly it would need to present consolidated financial statements.**

17. This case can be illustrated as follows:



According to the submitter’s view, Entity A prepares separate financial statements, which measure Entity B and Entity C at fair value. In addition, the submitter thinks that Entity B needs to prepare consolidated financial statements that will include Entity E and Entity F.

18. The submitter thinks that, if Entity B does meet the definition of an investment entity, paragraph 31 and paragraph 4 (c) are applicable to Entity B and, consequently, Entity B does not need to present consolidated financial statements.

4 An entity that is a parent shall present consolidated financial statements. This IFRS applies to all entities, except as follows:

(c) an investment entity need not present consolidated financial statements if it is required, in accordance with paragraph 31 of this IFRS, to measure all of its subsidiaries at fair value through profit or loss.

19. However we think that, if Entity B does not meet the definition of an investment entity, Entity B will need to present consolidated financial statements, because paragraph 4(a) (iv) of IFRS 10 is applicable only if “*its ultimate or any intermediate parent produces consolidated financial statements.*” We think that this is contrary to the Board’s intention. Whether the investment entity parent has a subsidiary which provides investment-related services or not should not change the availability of the exemption. Accordingly, we think that paragraph 4 of IFRS 10 should be amended so that the exemption from presenting consolidated

financial statements would be applicable to all subsidiaries of an investment entity parent, assuming that the other criteria in IFRS 10 paragraph 4 are met.

Summary of outreach conducted

20. We asked IOSCO, ESMA and national standard-setters to provide information on the issue raised in the submission by posing the following questions to them:
- (a) *Q1. How common are each of these issues? If these are common, could you provide us with information that the Interpretations Committee could use to assess how widespread the issues are?*
 - (b) *Q2. In your view, is there diversity in practice in interpreting each issue? Please describe the predominant approach that you observe in practice.*

Responses from regulators and national standard-setters

21. We received responses from the following 14 jurisdictions: Europe (4), Asia (3), Americas (3), Oceania (1), Africa (1) and International (2).
22. Most of the respondents stated that they have limited experience of the Investment Entities Amendments, because entities are not required to apply the amendments until the annual period on or after 1 January 2014. However, most of the respondents with experience of the issue are aware of it and stated that they think the issue could cause diversity in practice.

Predominant approach followed in jurisdictions

23. Although we have received only a limited response on the predominant approach followed in jurisdictions, those who did respond supported View B in the submission.

Assessment against the interpretations agenda criteria

Agenda criteria	
We should address issues (5.16):	
that have widespread effect and have, or are expected to have, a material effect on those affected.	Yes. Entities are not required to apply the amendments until the annual period on or after 1 January 2014. Accordingly, the issue is not common in all jurisdictions at

Agenda criteria	
	this point. However, on the basis of our analysis from the outreach, we expect that this issue would be widespread and could have a material effect on those affected.
where financial reporting would be improved through the elimination, or reduction, of diverse reporting methods.	Yes. We think that it is necessary to amend paragraph 4 of IFRS 10, to clarify that all subsidiaries of an investment entity need not present consolidated financial statements.
that can be resolved efficiently within the confines of existing IFRSs and the <i>Conceptual Framework for Financial Reporting</i> .	Yes. Amendments to IFRS 10 can resolve the issue.
In addition:	
Is the issue sufficiently narrow in scope that the Interpretations Committee can address this issue in an efficient manner, but not so narrow that it is not cost-effective for the Interpretations Committee to undertake the due process that would be required when making changes to IFRSs (5.17)?	Yes. Narrow-scope amendments to IFRS 10 can resolve the issue.
Will the solution developed by the Interpretations Committee be effective for a reasonable time period (5.21)? (The Interpretations Committee will not add an item to its agenda if the issue is being addressed in a forthcoming Standard and/or if a short-term improvement is not justified).	Yes. The issue does not relate to a current or planned IASB project.
In addition to the implementation and maintenance criteria, an AIP should (6.11, 6.12):	
Replace unclear wording Provide missing guidance Correct minor unintended consequences, oversights or conflict	Yes. The issue is unintended oversights.
Not change an existing principle or propose a new principle	No. It does not change an existing principle or propose a new principle.
Not be so fundamental that the IASB will have to meet several times to conclude (6.14)	No. The issue is mere correction of unintended oversights, accordingly, it will not be so fundamental that the IASB will have to meet several times to conclude.

Staff recommendation

24. We recommend that the Interpretations Committee should not take the first issue onto its agenda, because the existing Standards sufficiently address the issue as discussed above.
25. We also recommend that the Interpretations Committee should take the second issue onto its agenda in the Annual Improvements. If the Interpretations

Committee agrees to propose an amendment, we will bring proposed wording to a future meeting.

Question for the Interpretations Committee

1. Does the Interpretations Committee agree with the staff's recommendation that the Interpretations Committee should not take the first issue onto its agenda?

Does the Interpretations Committee have any comments on the proposed wording in Appendix A for the tentative agenda decision?

2. Does the Interpretations Committee agree with the staff's recommendation that the Interpretations Committee should take the second issue onto its agenda as a narrow-scope amendment?

Appendix A—Proposed wording for tentative agenda decision

A1 The proposed wording for the tentative agenda decision is presented below.

IFRS 10 Consolidated Financial Statements: Investment Entities Amendments—The interaction between the investment entity amendments and the exemption from preparing consolidated financial statements requirements in IFRS 10

The Interpretations Committee received a request to clarify whether a relief that a parent need not present consolidated financial statements, which is available for non-investment entities, is applicable to entities affected by the Investment Entities amendments.

IFRS 10 *Consolidated Financial Statements* (2012) requires a parent entity to present consolidated financial statements. However, paragraph 4 of IFRS 10 provides an exemption that a parent need not present consolidated financial statements if “its ultimate or any intermediate parent produces consolidated financial statements that are available for public use and comply with IFRSs.”

If an investment entity has a subsidiary that provides investment-related services or activities, the investment entity consolidates the subsidiary, in accordance with paragraph 32 of IFRS 10. In these consolidated financial statements, subsidiaries providing investment-related services or activities are consolidated, but other investees are measured at fair value. Consequently, some subsidiaries are included in the consolidated financial statements at fair value. The question raised is whether the exemption under paragraph 4 of IFRS 10 is available to a subsidiary of an investment entity that has subsidiaries.

The Interpretations Committee noted that paragraph 4(a) (iv) of IFRS 10 requires that consolidated financial statements are prepared and does not specify how an entity must be included with parent’s consolidated financial statements. Accordingly, the Interpretations Committee considered that a parent entity, whose own parent (or ultimate parent) prepares consolidated financial statements, is eligible to use the exemption from preparing consolidated financial statements set out in paragraph 4(a) (iv) of IFRS 10, even if its parent (or ultimate parent) is an investment entity.

The Interpretations Committee considered that in the light of its analysis of the existing IFRS requirements, neither an interpretation nor an amendment to a Standard was necessary and consequently [decided] not to add the issue to its agenda.