



4 October 2011

## Investment Entities proposals could have far-reaching impacts

In September 2011 the Australian Accounting Standards Board (AASB) issued ED 220, which incorporates International Accounting Standards Board (IASB) ED/2011/4 *Investment Entities*.

ED/2011/4 proposes that investment entities meeting particular criteria should be required to account for investments in their controlled entities at fair value through profit or loss, rather than by consolidating them. ED/2011/4 also proposes changing the availability of the fair value option for investments in associates and joint ventures by limiting the measurement of associates and joint ventures at fair value through profit or loss to investment entities only.

The AASB Chairman, Kevin Stevenson expressed a number of concerns about the proposals.

It is unusual for a member of the AASB such as myself to express concerns about an exposure draft before submissions are received. But I do so on this occasion because this draft raises fundamental questions about existing requirements. In my view it could lead to increased use of off-balance-sheet accounting, see us depart from the concept of control and lead to unjustified changes in requirements accounting for associates and joint ventures. The exposure draft seeks to include in IFRS accounting practices previously used in North America and would be a step back from the universal consolidation model that we have followed. In this regard, I note that three IASB members have expressed alternative views on ED/2011/4.

Until now our stance has been that if an entity controls one or more entities, it should present consolidated financial statements because they are most likely to provide useful information about the economic entity to the greatest number of users. The exposure draft would replace that information with the fair value for the investment in a certain type of subsidiary. Will that be an improvement in Australian reporting? If fair value of the investment provides information, would not a better answer be disclosure of the fair value of the investment as well as consolidation? Even if the proposals have merit, is the definition of an investment entity robust enough to avoid exploitation?

Some might find the proposals superficially appealing because they might reduce the task of financial reporting for a group, but respondents need to be aware that the proposals would, as well as raising the spectre of creative structuring, also change the exemptions from applying equity accounting. Some entities that presently elect to fair value their investments in associates and joint ventures would find they can no longer do so, and this would potentially include, for example, insurers with assets held to back investment-linked insurance contracts.

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## Media Release

The AASB needs to hear very clearly from constituents whether this proposed standard is in the interest of Australian reporting and if it is not considered to be, we need to respond strongly to the IASB. I would encourage very active consideration of the proposals.

Comments are due to the AASB by 30 November 2011 and to the IASB by 5 January 2012 and Australian constituents are strongly encouraged to carefully review the proposals and make their views known to the AASB and the IASB.

### Background

ED/2011/4 proposes 'investment entities' be required to measure investments in controlled entities at fair value through profit or loss (rather than consolidate them). However, a non-investment entity parent of an investment entity would be required to consolidate the investment entity subsidiary and its controlled entities.

Investment entities are those meeting six specified criteria.

In addition, ED/2011/4 proposes to amend IAS 28 *Investments in Associates and Joint Ventures* to require investment entities to measure investments in associates or joint ventures at fair value through profit or loss. Other entities would need to apply equity accounting.

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