International Financial Reporting Standard

Investment Entities

October 2012

BASIS FOR CONCLUSIONS – AMENDMENTS

[IFRS 1, 3, 5, 9, 10, 12 & 13 and IAS 27, 28 & 39]

[Related to AASB 2013-5]

Amendments to the Basis for Conclusions on IFRS 10 *Consolidated Financial Statements*

Paragraphs BC8 and BC206 are footnoted with the following text and the heading above paragraph BCZ22 and paragraphs BCZ22–BCZ28 are deleted.

Investment Entities (Amendments to IFRS 10, IFRS 12 and IAS 27), issued in October 2012, introduced an exception to the principle that all subsidiaries shall be consolidated. The amendments define an investment entity and require a parent that is an investment entity to measure its investments in particular subsidiaries at fair value through profit or loss instead of consolidating those subsidiaries. These amendments are discussed in paragraphs BC215–BC317.

After paragraph BC214, headings and paragraphs BC215–BC317 are added.

Exception to consolidation for investment entities (2012 amendments)

Background

BC215 In October 2012, the Board issued *Investment Entities* (Amendments to IFRS 10, IFRS 12 and IAS 27), which provides an exception to consolidation for a class of entities that are defined as 'investment entities'. The Board added the Investment Entities project to its agenda in the course of its deliberations on IFRS 10 as a response to the comments received on ED 10.

BC216 The Board had considered this issue previously. In 2002, the respondents to the Exposure Draft of IAS 27 asked the Board to provide an exception to consolidation for the subsidiaries of venture capital organisations, private equity entities and similar organisations. At that time, the Board decided not to introduce such an exception because it did not think that it should differentiate between the types of entity, or the types of investment, when applying a control model of consolidation. It also did not agree that management's reasons for holding an investment should determine whether or not that investment is consolidated. The Board concluded that for investments under the control of venture capital organisations, private equity entities and similar organisations, users' information needs are best served by financial statements in which those investments are consolidated, thus revealing the extent of the operations of the entities they control.

BC217 The scope of the proposals in ED 10 was the same as the scope of the proposals in IAS 27. IAS 27 required reporting entities to consolidate all controlled entities, regardless of the nature of the reporting entity. Respondents to ED 10 questioned the usefulness of financial statements of investment entities that consolidate investees that the investment entity controls. They pointed out that some national accounting requirements, including United States Generally Accepted Accounting Principles (US GAAP), have historically provided industry–specific guidance that requires investment entities to measure all of their investments, including those that they control, at fair value. The respondents argued that an investment entity holds investments for the sole purpose of capital appreciation, investment income (such as dividends or interest), or both. Users of the financial statements of these investment entities told the Board that the fair value of the investments and an understanding of how the investment entity measures the fair value of its investments is the most useful information.

BC218 Furthermore, respondents to ED 10 argued that consolidated financial statements of an investment entity may hinder users' ability to assess an investment entity's financial position and results, because it emphasises the financial position, operations and cash flows of the investee, rather than those of the investment entity. Often, an investment entity holds non-controlling interests in some entities that are reported at fair value, as well as controlling interests in other entities that are consolidated in accordance with current principles in IFRSs. Reporting investments on more than one basis hinders comparability within the financial statements, because all investments are held by an investment entity for a similar purpose—returns from capital appreciation, investment income, or both. In addition, some of the items consolidated may be measured at historical cost, which distorts the performance assessment of the investment entity and does not reflect the way in which the business of the entity is managed.

BC219 Respondents to ED 10 also argued that when an investment entity consolidates entities that it controls, it is not required to provide the disclosures related to fair value measurements that would be required if the subsidiaries were measured at fair value. For example, IFRS 7 *Financial Instruments: Disclosures* relates only to recognised financial assets and liabilities. There is no requirement to provide disclosures related to fair value for investments in consolidated subsidiaries. Information about fair value and the methodology and inputs used for determining fair value is vital for users to make investment decisions about investment entities. Investors in an investment entity are interested in the fair value of their interest in that entity and often transact with it on a fair value basis (ie their investment in the investment entity is based on a share of the net assets of that entity). Reporting the fair value of substantially all of the net assets of an investment entity allows the investors in that entity to more easily identify the value of their share of those net assets.

BC220 In response to this feedback, the Board published an Exposure Draft *Investment Entities* (*Investment Entities* ED) in August 2011. The *Investment Entities* ED proposed that investment entities would be required to measure their investments in subsidiaries (except those subsidiaries that provide investment–related services) at fair value through profit or loss in accordance with IFRS 9 *Financial Instruments* (or IAS 39, if IFRS 9 has not yet been adopted). The majority of respondents to the *Investment Entities* ED broadly supported the proposed exception to consolidation for the reasons outlined in paragraphs BC217–BC219.

BC221 The Board conducted its deliberations leading to the publication of the *Investment Entities* ED and the final investment entities requirements jointly with the FASB. The similarities and differences between the investment entities guidance in IFRS and US GAAP are discussed further in paragraphs BC289–BC291.

Scope of the project

BC222 The *Investment Entities* ED proposed a limited-scope exception to consolidation for investment entities. A number of respondents to the *Investment Entities* ED asked the Board to expand the scope of its proposals.

BC223 Some respondents asked the Board to expand the scope of the project to require an investment entity to measure all of its investments at fair value. However, the Board noted that, in most cases, existing IFRSs require or permit investments held by an investment entity to be measured at fair value. For example an entity:

(a) may elect the fair value option in IAS 40 *Investment Property*; and

(b) would be required to measure its financial assets at fair value through profit or loss in accordance with IFRS 9 (or IAS 39) when those assets are managed on a fair value basis.

Consequently, the Board decided to limit the scope of the project to only providing an exception to consolidation for investment entities.

BC224 Other respondents requested an extension of the proposed exception to consolidation. In particular, respondents from the insurance industry requested an exception to consolidating their interests in insurance investment funds. They argued that presenting the fair value of their interests in insurance investment funds as a single line item, along with a single line item for the current value of their liability to policyholders who receive the returns from those investment funds, would provide more useful information to users than consolidation. The Board noted that providing an exception to consolidation for insurers' interests in insurance investment funds is outside the scope of the Investment Entities project, which was meant to provide an exception to consolidation for investment entities. In addition, any additional exceptions to consolidation would require the Board to do further work to define the entities that could apply those exceptions. The Board noted that this additional exception to consolidation was not contemplated in the scope of the project nor was it exposed for comment. Consequently, the Board decided not to extend the proposed exception to consolidation.

BC225 Other respondents asked the Board to provide guidance permitting an investor in an investment entity to use the reported net asset value (NAV) per share of that investment entity as a practical expedient for measuring the fair value of its investment in that investment entity. Similar guidance exists in US GAAP. The Board considered providing such a practical expedient in their deliberations on IFRS 13 *Fair Value Measurement* but decided against it because, at the time, there was no specific accounting guidance for investment entities in IFRS and because there are different practices for calculating NAVs in jurisdictions around the world. The Board decided that it is outside the scope of the Investment Entities project to provide fair value measurement guidance for investments in investment entities. The Board developed the definition of an investment entity to identify which entities should qualify for an exception to consolidation. The definition was not designed to decide which entities should qualify for a fair value measurement practical expedient. Moreover, the Board still has concerns that NAV could be calculated differently in different jurisdictions. Consequently, the Board decided not to provide an NAV practical expedient for fair value measurement as part of the Investment Entities project.

BC226 The Board has decided to adopt an entity-based approach to the exception to consolidation. That is, the exception to consolidation is based on the type of entity that owns the subsidiary. The Board considered providing an asset-based approach to the exception to consolidation. Under an asset-based approach, an entity would consider its relationship with, and the characteristics of, each of its subsidiaries (that is, each individual asset) to decide whether fair value measurement is more appropriate than consolidation. However, the Board decided to retain the entity-based exception to consolidation that was proposed in the

Investment Entities ED. The Board was concerned that an asset-based approach would significantly broaden the exception to consolidation by making the exception available to any entity holding relevant assets. This would represent a significant conceptual change to the consolidation model that the Board has developed in this IFRS. In addition, the Board believes that investment entities have a unique business model that makes reporting subsidiaries at fair value more appropriate than consolidation. An entity-based approach captures the unique business model of investment entities.

BC227 The Board also considered providing an option to allow investment entities to either consolidate subsidiaries or measure them at fair value through profit or loss. However, the Board believes that providing this option would be inconsistent with their view that fair value information is the most relevant information for all investment entities. Moreover, providing an option would reduce comparability between different investment entities. Consequently, the Board decided that an investment entity should be required to measure its subsidiaries at fair value through profit or loss.

Approach to assessing investment entity status

BC228 In the *Investment Entities* ED, the Board proposed six criteria that must be met in order for an entity to qualify as an investment entity. These criteria were based on guidance in US GAAP (Topic 946 *Financial Services—Investment Companies* in the *FASB Accounting Standards Codification®*).

BC229 Many respondents expressed concern that requiring an entity to meet all six criteria proposed in the *Investment Entities* ED would be too prescriptive. They thought that the proposed criteria inappropriately focused on the structure of an investment entity rather than on its business model and did not allow for the use of judgement in determining whether an entity is an investment entity. These respondents stated that a less prescriptive approach to assessing the criteria would result in more consistent reporting by entities with similar business models.

BC230 In addition, many respondents argued that the six proposed criteria in the *Investment Entities* ED did not provide a general description of an investment entity and an explanation of why fair value measurement is more relevant for the subsidiaries of an investment entity. Because the concept of an investment entity is new to IFRS, those respondents argued that the guidance should include a more general definition of an investment entity (rather than merely criteria to be an investment entity) and a justification for the exception to consolidation.

BC231 In response to the comments from respondents, the Board decided to provide a definition of an investment entity based on some of the criteria originally proposed in the *Investment Entities* ED. An entity that meets the definition of an investment entity would not consolidate its controlled subsidiaries (other than those subsidiaries that provide investment-related services or activities).

BC232 The Board agreed with respondents who stated that some of the proposed criteria were too strict and would inappropriately exclude some structures from qualifying as investment entities. The Board believes that there are structures in practice in which an entity does not meet one or more of the criteria that were described in the *Investment Entities* ED, but should still qualify as an investment entity. For example, the *Investment Entities* ED required an investment entity to have more than one investor; the Board thinks that some pension funds, sovereign wealth funds, and other investment funds with a single investor should qualify as investment entities. Moreover, respondents commented that the application guidance in the *Investment Entities* ED provided too many exceptions to the strict criteria.

BC233 Consequently, the Board decided that an entity would not be required to satisfy the remaining criteria to meet the definition of an investment entity and qualify for the exception to consolidation. However, the Board noted that the remaining criteria represent typical characteristics of an investment entity and decided to include these typical characteristics in the investment entities guidance to help entities determine whether they qualify as an investment entity. If an entity does not display one or more of the typical characteristics, it indicates that additional judgement is required in determining whether the entity meets the definition of an investment entity. Consequently, the Board also decided that an investment entity that does not have one or more of the typical characteristics would be required to disclose how it still meets the definition of an investment entity.

BC234 The Board thinks that it is very unlikely that an entity that displays none of the typical characteristics of an investment entity would meet the definition of one. However, it may be possible in rare circumstances. For example, a pension fund that has a single investor and does not issue equity ownership interests could qualify as an investment entity even if it only holds a single investment temporarily (eg at commencement or wind-down of the entity).

BC235 The Board believes that defining an investment entity and describing its typical characteristics achieves a balance between clearly defining those entities that qualify for the exception to consolidation and avoiding the use of bright lines. In addition, this approach allows the definition to stand on its own, with application guidance providing clarification rather than exceptions.

Definition of an investment entity

BC236 The definition of an investment entity has three essential elements that differentiate investment entities from other types of entities.

Investment management services

BC237 The Board noted that one of the essential activities of an investment entity is that it obtains funds from investors in order to provide those investors with investment management services. The Board believes that this provision of investment management services differentiates investment entities from other entities. Consequently, the Board decided that the definition of an investment entity should state that an investment entity obtains funds from an investor or investors and provides the investor(s) with investment management services.

Business purpose

BC238 The Board believes that an entity's activities and business purpose are critical to determining whether it is an investment entity. An investment entity collects funds from investors and invests those funds to obtain returns solely from capital appreciation, investment income, or both. Consequently, the Board decided that the definition of an investment entity should state that an investment entity commits to its investor(s) that its business purpose is to provide investment management services and invest funds solely for returns from capital appreciation, investment income, or both.

BC239 The *Investment Entities* ED did not allow an entity to qualify as an investment entity if it provided substantive investment-related services to third parties. While some respondents agreed with this, others argued that an investment entity should be allowed to provide such services to third parties. They argued that the provision of these investment-related services to third parties is simply an extension of the investment entity's investing activities and should not prohibit an entity from qualifying as an investment entity. The Board agreed with these arguments, concluding that the provision of such services is within the business model of an investment entity. Although such an entity may earn fee income from the provision of investment-related services, its sole business purpose is still investing for capital appreciation, investment income, or both (whether that is for itself, for its investors or for external parties).

BC240 The Board noted that an investment entity may sometimes hold an interest in a subsidiary that provides investment-related services for its investment activities. The Board did not think that the existence of such a subsidiary should prohibit an entity from qualifying as an investment entity, even if those services were substantial or were provided to third parties in addition to the entity. The Board views such services as an extension of the operations of the investment entity and therefore concluded that subsidiaries that provide those services should be consolidated.

BC241 The Board considered prohibiting investment entities from engaging in some activities, such as providing financial support to its investees or actively managing its investees. However, the Board understands that an investment entity may engage in these activities in order to maximise the overall value of the investee (ie to maximise capital appreciation), rather than to obtain other benefits. Consequently, the Board believes that these activities can be consistent with the overall activities of an investment entity and should not be prohibited as long as they do not represent a separate substantial business activity or source of income other than capital appreciation.

BC242 The Board was concerned that an entity that meets the definition of an investment entity could be inserted into a larger corporate structure to achieve a particular accounting outcome. For example, a parent entity could use an 'internal' investment entity subsidiary to invest in subsidiaries that may be making losses (eg research and development activities on behalf of the overall group) and would record its investments at fair value, rather than reflecting the underlying activities of the investee. To address these concerns and to emphasise the business purpose of an investment entity, the Board decided to include a requirement that an investment entity, or other members of the group containing the entity, should not obtain benefits from its investees that would be unavailable to other parties that are not related to the investee. In the Board's view, this is one of the factors that differentiate an investment entity from a non-investment entity holding company. If an entity or another member of the group containing the entity obtains benefits from its investees that are unavailable to other investors, then the investment will benefit that entity or the group in some operating or strategic capacity and the entity will therefore not qualify as an investment entity.

BC243 However, the Board also clarified that an investment entity may have more than one investment in the same industry, market or geographical area in order to benefit from synergies that increase the capital appreciation of those investments. It noted that such a fact pattern may be common in the private equity industry. Some Board members expressed concern that allowing transactions or synergies between investments may artificially increase the fair value of each investment and, consequently, inappropriately increase the assets reported by the investment entity. However, the Board decided that trading transactions or synergies that arise between the investments of an investment entity should not be prohibited because their existence does not necessarily mean that the investment entity is receiving any returns beyond solely capital appreciation, investment income, or both.

Exit strategy

BC244 The Board believes that a parent with operating subsidiaries often plans to own and operate its subsidiaries indefinitely to realise returns from those operations. However, the Board does not think that an entity that holds its investments indefinitely, especially its subsidiaries, should qualify as an investment entity. Accordingly, the Board considered requiring an exit strategy for substantially all investments held by an investment entity, including debt investments.

BC245 However, respondents to the *Investment Entities* ED noted that some investment funds that would otherwise qualify as investment entities may hold a significant amount of debt investments to maturity and therefore would not have an exit strategy for those debt investments. For example, the Board understands that, in some cases, private equity funds may make both debt and equity investments in their investees. The debt investments may have shorter maturities than the anticipated term of the fund's equity investment and may be held to maturity. Moreover, an investment entity may hold debt instruments to maturity to manage liquidity risk or to mitigate the risk from holding other types of more volatile investments. Although the entity does not have an exit strategy for these debt investments, it does not plan to hold them indefinitely—even if the entity does not plan to sell these investments before maturity, the vast majority of debt investments have a limited life.

BC246 The Board decided that such an entity should not be prohibited from qualifying as an investment entity, provided that substantially all of its investments (including debt investments) are measured at fair value. The Board noted that debt investments may be measured at fair value in accordance with IFRS 9 or IAS 39 even in the absence of an exit strategy.

BC247 However, the Board decided that an investment entity must have an exit strategy for substantially all of its investments that can be held indefinitely (typically equity investments and non-financial assets). The Board does not think it is appropriate for an entity to qualify for an exception to consolidation if that entity is holding equity investments indefinitely and is not planning to realise capital appreciation from those investments. Although the exit strategy may vary depending on circumstances, potential exit strategies that include a substantive time frame for exiting from the investment should still be identified and documented for equity and non-financial investments in order to meet the definition of an investment entity.

BC248 The Board noted that an entity may fail to meet this component of the definition of an investment entity if it is formed in connection with an investment entity investee for legal, regulatory, tax or similar business reasons (eg a 'blocker' entity or a 'master-feeder' structure), and that that investee holds investments on behalf of the entity. The Board decided that the entity should not be prohibited from qualifying as an investment entity merely because it does not have an exit strategy for the investee, if that investee qualifies as an investment entity and has appropriate exit strategies for its own investments.

Fair value measurement

BC249 In the development of IFRS 10 and the *Investment Entities* ED, the Board heard that fair value information is the primary driver of the decision-making processes both of the management of, and the investors in, investment entities. Many respondents stated that both management and investors evaluate the performance of an investment entity by reference to the fair value of its investments. The Board heard that some investors in investment entities disregard the consolidated financial statements of investment entities and instead rely on non-GAAP fair value reports.

BC250 The basis for the exception to consolidation that is provided to investment entities is that fair value information is the most relevant for an investment entity's investments, including its investments in subsidiaries. The Board therefore decided that an essential feature of the definition of an investment entity is that the entity would use existing IFRS requirements or accounting policy options to measure substantially all of its investments at fair value. The Board does not think that an entity that fails to elect the fair value measurement options available in IAS 28 *Investments in Associates and Joint Ventures* or IAS 40, or that accounts for more than an insignificant amount of its financial assets at amortised cost under IFRS 9 or IAS 39, should qualify as an investment entity.

BC251 The Board noted that some investments may be measured at fair value in the statement of financial position, with fair value changes recognised in other comprehensive income rather than through profit or loss, and agreed that this would satisfy the fair value measurement element of the definition of an investment entity.

BC252 The Board considers that a significant distinguishing characteristic of an investment entity is that investors in an investment entity are primarily interested in fair value and make their investing decisions based on the fair value of the investment entity's underlying investments. The Board notes that this is partly because, in many cases, investors in an investment entity transact with it on a fair value basis (for example, on the basis of a net asset value per share, which is calculated using the fair value of the entity's underlying investments). Similarly, the Board believes that fair value should also be used by an investment entity's key management personnel to assess the entity's performance and to make investing decisions. Consequently, the Board decided that, in order to meet the definition of an investment entity, an entity should demonstrate that fair value is the primary measurement attribute used to evaluate the performance of its investments, both internally and externally.

Regulatory requirements

BC253 The Board considered whether to include a reference to regulatory requirements in the definition of an investment entity. The Board noted that the FASB proposed, in their own Exposure Draft, that any entity that was regulated as an investment company under the US Securities and Exchange Commission's Investment Company Act of 1940 would automatically be considered to be an investment company for US GAAP financial reporting purposes. Some respondents to the Board's *Investment Entities* ED also asked the Board to include a reference to regulatory requirements in the definition of an investment entity, which would allow any entity regulated as an investment entity to fall within the scope of the investment entity requirements.

BC254 However, the Board was concerned that:

(a) the regulatory requirements in different jurisdictions may result in similar entities qualifying as an investment entity in one jurisdiction but not in another;

(b) regulatory requirements may change over time, resulting in an ever-changing population of entities that would be eligible for an exception to consolidation; and

(c) it would have no control over which entities would qualify for the exception to consolidation.

Consequently, the Board decided not to reference regulatory requirements in the definition of an investment entity.

Typical characteristics of investment entities

BC255 The Board identified several 'typical characteristics' of an investment entity. The Board decided that these typical characteristics could be used to help an entity decide if it meets the definition of an investment entity. The absence of any of these typical characteristics may indicate that an entity does not meet the definition of an investment entity. However, an entity that does not display all of these typical characteristics could, nevertheless, meet the definition of an investment entity.

BC256 The Board identified the following typical characteristics of an investment entity:

(a) more than one investment (paragraphs BC257–BC258);

(b) more than one investor (paragraphs BC259–BC260);

(c) unrelated investors (paragraphs BC261–BC262); and

(d) ownership interests (paragraphs BC263–BC267).

More than one investment

BC257 The *Investment Entities* ED proposed that an investment entity should hold more than one investment. However, respondents provided examples of entities that they believed should qualify as investment entities, but that only hold a single investment. These included single investment funds set up because the required minimum investment is too high for individual investors, or investment funds that hold a single investment temporarily.

BC258 The Board agreed with these arguments and therefore decided that an investment entity would not be required to hold more than one investment. However, the Board understands that investment entities typically invest in more than one investment as a means of diversifying their portfolio and maximising their returns. Consequently, investing in more than one investment is described as a typical characteristic of an investment entity in this IFRS.

More than one investor

BC259 The presence of more than one investor was originally proposed as a requirement in the *Investment Entities* ED. However, respondents provided many examples of investment funds with a single investor. These included funds that temporarily have a single investor, government-owned investment funds, funds wholly-owned by pension plans and endowments, and funds set up by an investment manager for an unrelated single investor with a unique investment strategy.

BC260 The Board does not think that there is a conceptual reason why an investment fund with a single investor should be disqualified from being an investment entity. However, the Board thinks that having more than one investor would make it less likely that the entity, or other members of the group that contains the entity, would obtain benefits other than capital appreciation or investment income from its investment. Consequently, the Board decided to include the presence of more than one investor as a typical characteristic of an investment entity rather than as part of the definition of an investment entity.

Unrelated investors

BC261 The *Investment Entities* ED proposed that an investment entity be required to have investors that are unrelated to the entity or its parent (if any), partly to prevent entities from structuring around the requirement to have more than one investor. However, respondents provided examples of entities with related investors that they believed should qualify as investment entities. For example, a separate 'parallel' entity may be formed to allow the employees of an investment entity to invest in a fund that mirrors the investments in the main fund. The Board agreed with the respondents' arguments and decided that an investment entity would not be required to have investors that are unrelated to the investment entity or to other members of the group that contains the investment entity.

BC262 However, the Board understands that investment entities typically have unrelated investors. Again, having unrelated investors is one way to help ensure that the entity, or another member of the group that contains the entity, does not receive returns from investments that are other than capital appreciation or investment income. Having investors that are unrelated to the entity or its parent (if any), is therefore described as a typical characteristic of an investment entity in this IFRS.

Ownership interests

BC263 An investment entity would typically have ownership interests in the form of equity or similar (eg partnership) interests that entitle investors to a proportionate share of the net assets of the investment entity. This characteristic explains in part why fair value is more relevant to investment entity investors: each unit of ownership in the investment entity entitles an investor to a proportionate share of the net assets of that investment entity. The value of each ownership interest is linked directly to the fair value of the investment entity's investments.

BC264 However, the Board believes that this form of ownership interests in an entity should not be the deciding factor as to whether it is an investment entity. Respondents provided examples of entities that do not have units of ownership in the form of equity or similar interests but provide investors with a proportionate share of their net assets. For example, a pension fund or sovereign wealth fund with a single direct investor may have beneficiaries that are entitled to the net assets of the investment fund, but do not have ownership units. In addition, respondents noted that funds with different share classes or funds in which investors have discretion to invest in individual assets would be disqualified from investment entity status because they did not provide each investor with a proportionate share of net assets.

BC265 The Board does not believe that an entity that provides its investors only a return of their investment plus interest should qualify as an investment entity. Fair value information is more relevant to investors that are entitled to a specifically identifiable portion of the investment entity's net assets and are, therefore, exposed to the upside and downside of the investment entity's performance.

BC266 However, the Board agreed that the requirement proposed in the *Investment Entities* ED (that an investment entity's ownership interests entitle investors to a proportionate share of its net assets) would have inappropriately excluded certain structures from investment entity status. As an alternative, the Board considered requiring that an investment entity's ownership interests be in the form of equity or similar interests. However, the Board was concerned that this would put too much emphasis on the debt/equity classification in IAS 32 *Financial Instruments: Presentation* and would inappropriately exclude some structures whose ownership interests were classified as debt. Moreover, the Board was also concerned that including the 'ownership interest' concept as part of the definition of an investment entity would put too much emphasis on the form of the entity, rather than emphasising its business model.

BC267 Consequently, the Board decided not to include ownership interests as part of the definition of an investment entity but that it should instead be regarded as a typical characteristic of an investment entity.

Reassessment and change of status

BC268 The Board included guidance in the *Investment Entities* ED on reassessing investment entity status. A few respondents asked the Board to clarify this guidance.

BC269 In the *Investment Entities* ED, the Board proposed that an entity would reassess its investment entity status whenever facts or circumstances changed. The Board decided to retain this requirement unchanged because it is consistent with the requirements for reassessment elsewhere in IFRS, including the general reassessment requirements in IFRS 10. The Board noted that they do not believe that the reassessment of facts and circumstances in other situations is considered unduly onerous for preparers or their auditors.

BC270 The Board decided that, when an entity loses investment entity status, it should account for that change as a 'deemed acquisition'. That is, the investment entity would use the fair value of the investment at the date of the change of status as the 'deemed' consideration transferred to obtain control of the investee. This recognises the change in status in the same way as a business combination achieved in stages, as described in IFRS 3. This would result in the recognition of goodwill or a gain on a bargain purchase.

BC271 The Board also decided that, when an entity becomes an investment entity, the entity should account for the change in status as a 'deemed disposal' or 'loss of control' of its subsidiaries. The fair value of the investment at the date of the change of status should be used as the consideration received when applying the guidance in IFRS 10. The Board considered how to account for the gain or loss on the 'deemed disposal' and decided to recognise it as a gain or loss in profit or loss. This treats the change in the business purpose of the investor as a significant economic event and is consistent with the rationale for gains and losses being recognised in profit or loss in IFRS 10 when control is lost.

Parent of an investment entity

Investment entity parent of an investment entity subsidiary

BC272 The *Investment Entities* ED proposed that an investment entity would measure all of its subsidiaries at fair value (except for those subsidiaries providing investment-related services), even those investees who were themselves investment entities. Some respondents questioned this proposal and suggested that at least some investment entity subsidiaries should be consolidated (for example, wholly-owned investment entity subsidiaries that are created for legal, tax or regulatory purposes). However, the Board thinks that fair value measurement of all an investment entity's subsidiaries (except for those subsidiaries providing investment-related services or activities) would provide the most useful information and therefore decided to retain this proposal. The Board considered requiring an investment entity to consolidate only those investment entity subsidiaries that are formed for legal, tax or regulatory purposes, but decided against this because there is no conceptual basis for distinguishing between different investment entity subsidiaries. Moreover, the Board thinks that it would be very difficult to distinguish between an investment entity subsidiary formed for a specific legal, tax or regulatory purpose and those that are set up only for other business reasons.

BC273 The Board considered whether it should require certain investment entity parents to attach the financial statements of their investment entity subsidiaries to the parent's financial statements. Some respondents argued that it would be essential for users of the financial statements of an investment entity parent to have information about the underlying investments of its investment entity subsidiary, particularly when the investment entity parent has only one investment entity subsidiary (eg 'master-feeder funds').

BC274 However, the Board decided against requiring financial statements of an investment entity subsidiary to be attached to the financial statements of an investment entity parent. The Board believed that it would be difficult to define which types of structures should be covered by such a requirement. Moreover, the Board thought that such a requirement would be inconsistent with the proposal that fair value information is always the most relevant information for investment entities.

Non-investment entity parent of an investment entity subsidiary

BC275 The Board also considered whether to retain investment entity accounting in the financial statements of a non-investment entity parent. In the *Investment Entities* ED, the Board proposed that a non-investment entity parent of an investment entity subsidiary would be required to consolidate all of its subsidiaries; that is, the exception to consolidation available to an investment entity would not be available to its non-investment entity parent.

BC276 The Board noted that the majority of respondents disagreed with the proposal, arguing that if fair value information is more relevant than consolidation at an investment entity subsidiary level, it is also more relevant information at the non-investment entity parent level.

BC277 The Board acknowledged the comments received but decided to retain the proposal to require all non-investment entity parents to consolidate all of their subsidiaries.

BC278 The Board has decided to provide an exception to consolidation because of the unique business model of investment entities. Non-investment entities do not have this unique business model; they have other substantial activities besides investing, or do not manage substantially all of their assets on a fair value basis. Consequently, the argument for a fair value measurement requirement is weakened at a non-investment entity level.

BC279 The Board also noted that the decision to define an investment entity and describe its typical characteristics rather than requiring an investment entity to meet a number of criteria has increased the population of entities that could qualify as investment entities, and has also increased the amount of judgement needed to determine whether an entity is an investment entity. For example, an entity with a single investor, or an entity that provides day-to-day management services or strategic advice to its subsidiary, can qualify as an investment entity under this IFRS, when such entities would have been excluded under the *Investment Entities* ED.

BC280 The Board was concerned that some of these changes would increase the likelihood that a non-investment entity parent could achieve different accounting outcomes by holding subsidiaries directly or indirectly through an investment entity. The Board noted that, for example, a non-investment entity parent may elect to hold subsidiaries through an investment entity subsidiary in order to hide leverage or loss-making activities.

BC281 In addition, the Board considered the practical difficulties in retaining the exception to consolidation when a non-investment entity parent and an investment entity subsidiary invest in the same investment or when an investment entity subsidiary holds a subsidiary that invests in the equity of a non-investment entity parent.

BC282 The Board noted that the retention of the specialised accounting used by an investment company subsidiary at a non-investment company level is a long-standing requirement in US GAAP. However, US GAAP has industry-specific guidance for a number of industries, and the application of that industry-specific guidance by a subsidiary is retained by a parent entity, regardless of whether the parent entity is part of that industry. IFRSs generally do not contain such industry-specific guidance.

BC283 Some respondents to the *Investment Entities* ED noted that not retaining the fair value accounting of an investment entity subsidiary in its non-investment entity parent's financial statements seems inconsistent with IAS 28 *Investments in Associates and Joint Ventures*. IAS 28 allows a parent that indirectly holds an investment in an associate through a venture capital organisation, mutual fund, unit trust or similar entity to measure that portion of the investment at fair value through profit or loss in accordance with IFRS 9 or IAS 39. The Board acknowledged the inconsistency but thought it was important to keep the retention of fair value accounting that is currently allowed for venture capital organisations, mutual funds, unit trusts and similar entities. The Board also noted that the difference between using the equity method and fair value measurement for investments in associates and joint ventures is smaller than that between consolidation and fair value measurement for investments in subsidiaries.

Transition

BC284 The Board proposed in the *Investment Entities* ED that the exception to consolidation should be applied prospectively. Some respondents disagreed with the proposal, arguing that retrospective application would result in more useful information. In addition, they noted that retrospective application should not be onerous because investment entities would be expected to have information about the fair value of their investments. Those respondents also argued that retrospective application would be consistent with the other transition requirements in IFRS 10.

BC285 The Board agreed with these arguments and decided to require retrospective application of the exception to consolidation, subject to specific transition reliefs, such as:

(a) a relief for when it is impracticable to identify the fair value of investments;

(b) a relief for when an investment entity disposes of investments prior to the date of initial application; and

(c) a relief from providing comparative information for more than one period preceding the date of initial application.

BC286 The Board also noted that entities that adopt these amendments early may not have adopted IFRS 13, which has an effective date of 1 January 2013. Consequently, the Board decided that when an investment entity has not yet adopted IFRS 13, it may use the fair value amounts previously reported to investors or to management, as long as those amounts represent the amount for which the investment could have been exchanged between knowledgeable, willing parties in an arm's length transaction at the date of the valuation. The Board noted that if previously used fair value measurements are not available, it may be impracticable to measure fair value without using hindsight. In such cases, transition relief is available.

BC287 The Board also decided to require first-time adopters to apply the requirements retrospectively, subject to specific transition reliefs.

Effective date and early application

BC288 The Board decided on a 1 January 2014 effective date for the requirements for investment entities. The Board noted that because these requirements provide an exception to consolidation, they should have the same effective date as the revised consolidation requirements in

IFRS 10 (annual periods beginning on or after 1 January 2013). However, given that the investment entities requirements were published in October 2012, the Board did not believe that a 1 January 2013 effective date would give adequate time for implementation between the publication and effective dates. However, the Board decided to permit early application of the investment entity requirements. The Board noted that it expects many entities to apply the requirements early. Some investments in subsidiaries may not have been consolidated in accordance with IAS 27 and SIC-12 but, without the exception to consolidation, would need to be consolidated in accordance with IFRS 10. The Board noted that it would be potentially confusing to users of financial statements and time-consuming for the investment entity to consolidate a subsidiary in one accounting period and then carry the same investee at fair value in the following period. In addition, investment entities should already have the fair value information needed for implementation. Finally, the exception to consolidation has been a long-standing request from the investment entity industry. Consequently, the Board believes that many investment entities will want to adopt the requirements early.

Joint deliberations with the FASB

BC289 The Board deliberated this project jointly with the FASB. US GAAP has had comprehensive accounting guidance for investment companies for many years (contained in Topic 946 *Investment Companies*). By deliberating this project jointly, the boards hoped to achieve as similar guidance as possible. To that end, they came up with similar definitions of investment entities and guidance on how to assess investment entity status.

BC290 However, the scope of the project was different for the IASB and the FASB. The IASB's Investment Entities project started during the deliberations on the Consolidations project and was only intended to provide an exception to consolidation for investment entities. The FASB was seeking to improve and converge the definition of an investment company with that of the IASB because it already has comprehensive accounting and reporting guidance for investment companies.

BC291 While the boards reached many common decisions, as a result of this scope difference, and other jurisdictional differences, the IASB and the FASB came to different decisions in a number of areas. These include:

(a) whether there should be a requirement that an investment entity measure and evaluate substantially all of its investments on a fair value basis rather than identifying such an activity as a typical characteristic of an investment entity;

(b) whether there should be a reference to existing regulatory requirements in the definition of an investment entity;

(c) whether an investment entity is permitted to provide investment-related services to third parties other than its own investors;

(d) the accounting by an investment entity parent for an investment entity subsidiary; and

(e) the accounting by a non-investment entity parent for an investment entity subsidiary.

Effects analysis for investment entities

BC292 The Board is committed to assessing and sharing knowledge about the likely costs of implementing proposed new requirements and the likely ongoing costs and benefits of each new IFRS—the costs and benefits are collectively referred to as 'effects'. The Board gains insight on the likely effects of the proposals for new or revised IFRSs through its formal exposure of proposals, analysis and consultations with relevant parties.

BC293 In evaluating the likely effects of introducing an exception to consolidation for investment entities to IFRS 10, the Board has considered the following factors:

(a) how the changes to IFRS 10 affect the financial statements of an investment entity;

(b) how those changes improve the comparability of financial information between different reporting periods for an investment entity and between different investment entities in a particular reporting period;

(c) how the changes will improve the quality of the financial information available to investors and its usefulness in assessing the future cash flows of an investment entity;

(d) how users will benefit from better economic decision-making as a result of improved financial reporting;

(e) the likely effect on compliance costs for preparers, both on initial application and on an ongoing basis; and

(f) whether the likely costs of analysis for users are affected.

Financial statements of investment entities

BC294 Before the exception to consolidation for investment entities was issued, IFRS 10 (and its predecessor, IAS 27) required reporting entities to consolidate all controlled entities, regardless of the nature of the reporting entity. Consequently, the assets, liabilities and non-controlling interests of each subsidiary were aggregated with those of the parent to represent the group of entities as a single reporting entity.

BC295 Respondents to ED 10 argued that an investment entity often holds non-controlling investments in some entities that are reported at fair value, as well as subsidiaries that are consolidated in accordance with current principles in IFRS. Reporting investments on more than one basis hinders comparability within the financial statements, because all investments are held by an investment entity for a similar purpose—capital appreciation, investment income, or both. In addition, some of the items consolidated would be measured at historical cost, which distorts the performance assessment of the investment entity and does not reflect the way in which the business of the entity is managed.

BC296 The exception to consolidation will change the way in which an investment entity parent reports its interest in an entity that it controls. Rather than consolidating its subsidiaries, an investment entity is now required to recognise a subsidiary as a single-line investment measured at fair value through profit or loss in accordance with IFRS 9 (or IAS 39, if IFRS 9 has not yet been adopted).

BC297 Accordingly, the exception to consolidation will affect investment entities that hold, as investments, controlling interests in other entities. However, although the changes are important to those entities affected, the changes are only expected to affect a narrow range of entities. Only those entities that meet the definition of an investment entity and hold controlling interests in other entities will be affected by these changes.

BC298 The entities most likely to be affected are:

(a) private equity or venture capital funds; these have business models in which it is more likely that it would be beneficial to take a larger interest in a company, or control investees through debt and equity investment.

(b) master-feeder or fund-of-funds structures where an investment entity parent has controlling interests in investment entity subsidiaries.

BC299 Some pension funds and sovereign wealth funds may also be affected; these may meet the definition of an investment entity and may also hold controlling investments in other entities.

BC300 Other types of entities may meet the definition of an investment entity, such as mutual funds and other regulated investment funds, but are less likely to hold controlling investments in other entities. Instead, they tend to hold lower levels of investments in a wider range of entities. Consequently, the exception to consolidation is less likely to affect these entities.

Comparability

BC301 An investment entity's control of an investee may change from one reporting period to the next. Without the exception to consolidation, an investment entity could be required to consolidate an investment in one period and present it as an investment measured at fair value through profit or loss in the following period (or vice versa). This would reduce comparability between reporting periods. With the introduction of the exception to consolidation, an investment entity can report all investments at fair value, regardless of whether those investments are controlled. This will improve the comparability between reporting periods.

BC302 Many respondents to ED 10 and the *Investment Entities* ED pointed out that some national accounting requirements, including US GAAP, have historically had industry-specific guidance that requires investment entities to measure investments that they control at fair value. Some of these respondents argued that investment entities were actively choosing to adopt those national accounting requirements rather than IFRS so that they could measure all of their investments at fair value. Respondents also pointed out that some investment entities that followed IFRS provided non-GAAP information about the fair value of all of their investments. Consequently, comparability of the financial statements of different investment entities was hindered. The Board expects the introduction of the exception to consolidation to encourage adoption of IFRS among investment entities and to eliminate the need to provide non-GAAP information about fair value. This should improve the comparability of financial statements of different investment entities.

Usefulness of financial statements in assessing the future cash flows of an entity

BC303 Consolidated financial statements of an investment entity emphasise the financial position, operations and cash flows of the investee, rather than merely those of the investment entity. The exception to consolidation will reduce the information about the cash flows of those subsidiaries. However, the main business purpose of an investment entity is to invest funds solely for capital appreciation, investment income, or both. The relevant cash flows relating to these activities are those of the investment entity itself. Consolidating the cash flows of a subsidiary may hinder users' ability to predict the cash flows that may be passed on to investors. The Board therefore believes that these amendments will improve the quality of the financial information reported by an investment entity and will make that information more useful in assessing the future cash flows of the investment entity.

Better economic decision-making

BC304 One of the essential features of an investment entity is that, in order to make better investment decisions, it measures and evaluates substantially all of its investments on a fair value basis. Presenting consolidated financial statements does not reflect this method of management. Requiring an investment entity to account for its investments in subsidiaries at fair value provides a better insight into the information that management uses to evaluate the performance of its investments.

BC305 In addition, investors in an investment entity are typically entitled to a proportionate share of the net assets of the entity when they withdraw their investment. Reporting the fair value of substantially all of the net assets of the investment entity allows the investors to more easily identify the value of their share of those net assets. As a result, the Board expect significant benefits for most users of investment entity financial statements arising from the provision of more fair value information.

BC306 However, some respondents in some jurisdictions objected to the exception to consolidation because it undermines the control-based approach to consolidation used in IFRS 10. These respondents noted that an exception to consolidation would deprive financial statement users of information about the activities of subsidiaries and the economic effects of the relationships between an investment entity and its subsidiaries. In addition, some respondents expressed concern that an exception to consolidation may encourage structuring to avoid consolidation, which would result in a loss of such information to users.

BC307 The Board acknowledges these arguments, but notes that the exception to consolidation has been introduced in response to comments from users that the most useful information for an investment entity is the fair value of its investments. Users also commented that consolidated financial statements of an investment entity may hinder users' ability to assess an investment entity's financial position and results, because it emphasises the financial position, operations and cash flows of the investee, rather than those of the investment entity.

BC308 In developing these amendments, the Board deliberately restricted the population of entities that would qualify for the exception to consolidation. In particular, the Board prohibited the use of the exception to consolidation by non-investment entity parents of investment entities, in order to address respondents' concerns about structuring and to restrict the use of the exception to situations where fair value information would be more relevant than information arising from the consolidation of subsidiaries.

Effect on compliance costs for preparers

BC309 The Board expects that the introduction of the exception to consolidation will result in significant compliance cost savings for preparers, particularly on an ongoing basis. This expectation is based on the feedback the Board has received from respondents to the *Investment Entities* ED and conversations with entities that are expected to qualify as investment entities.

BC310 On initial application, there may be some costs involved in identifying and documenting some of the additional disclosures introduced. In particular, investment entities will need to collect information to comply with the general disclosure requirements of IFRS 7, IFRS 13 and the amended requirements of IFRS 12. However, the Board has been told that the majority of investment entities will already have much of the fair value information that they need in order to comply with the new requirements, because they already measure substantially all of their investments on a fair value basis and many elect to provide this information to their investors already. The Board expects this to mitigate the initial and ongoing costs of applying the exception to consolidation.

BC311 In arriving at its decisions, the Board has considered those costs and believes that the benefits of the information produced as a result of its decisions would outweigh the costs of providing that information. In addition, the initial application costs will be more than offset by the cost savings resulting from the removal of the need to gather information from subsidiaries in order to consolidate details of their financial performance, position and cash flows on a line-by-line basis.

BC312 As described in paragraphs BC275–BC283, the Board decided not to expand the scope of the project to allow a non-investment entity parent to retain the fair value accounting of its investment entity subsidiary. Consequently, the compliance cost savings described above will not be available to non-investment entity parents. Because these entities are not within the scope of these amendments, they may incur ongoing costs because they will have two different bases of accounting within the group. At the investment entity subsidiary level, subsidiaries held by the investment entity will be measured at fair value, but at the non-investment entity parent level, those subsidiaries will be consolidated.

How the costs of analysis for users are affected

BC313 The likely effect of these amendments on the costs of analysis for users of financial statements is expected to be outweighed by the benefits of improved reporting, given that these amendments have been developed on request from users. However, the extent of the benefit will depend on existing practice.

BC314 In general, these amendments will provide improved information about the fair values of investments and the way in which the fair value is measured. Such information could reduce the cost of analysis by providing information more directly to users of financial statements. However, in many cases, investment entities already provide investors with fair value information, although this is often done in an alternative report rather than in the financial statements. This serves to emphasise that the main benefit of the changes is a reduction in costs to preparers because it eliminates what they see as a cumbersome reporting requirement that has little value.

BC315 For analysts or potential investors that use financial statements to analyse investment entities from different countries, the existing problems of diversity in accounting models creates costs that would be reduced by standardised accounting requirements.

BC316 In addition, the Board expects that the requirement to apply the exception to consolidation retrospectively will mitigate some of the transition costs for users. However, some of the transition reliefs will mean that users may receive less information on transition. In particular, the fact that investment entities will be required to provide only one period of comparative information may affect users who might otherwise receive more than one period of comparative information. However, again, the Board expects the benefits to outweigh the costs incurred as a result of the implementation of these amendments.

Summary

BC317 In summary, the cost savings resulting from implementing these amendments are expected to be significant for investment entities and the users of their financial statements. Additionally, the implementation of the investment entities amendments should result in the benefits of increased comparability between entities and across jurisdictions, and more relevant reporting of information used by investors in making economic decisions.

Appendix
Consequential amendments to the Basis for Conclusions on other Standards

This appendix contains amendments to the Basis for Conclusions on other Standards that are necessary in order to ensure consistency with Investment Entities *(Amendments to IFRS 10, IFRS 12 and IAS 27) and the related amendments to other IFRSs. Amended footnotes are shown with the new text underlined.*

IFRS 1 *First-time Adoption of International Financial Reporting Standards*

The heading above paragraph BC31 is footnoted with the following text.

In October 2012 the Board issued *Investment Entities* (Amendments to IFRS 10, IFRS 12 and IAS 27), which stated that Appendix C of IFRS 1 should only apply to business combinations within the scope of IFRS 3 *Business Combinations*.

In paragraph BC63 'if no adjustments were made for consolidation procedures and for the effects of the business combination in which the parent acquired the subsidiary.' is footnoted with the following text.

In October 2012 the Board issued *Investment Entities* (Amendments to IFRS 10, IFRS 12 and IAS 27), which removed option D16(a) for investments in subsidiaries of investment entities, as defined in IFRS 10 *Consolidated Financial Statements*, required to be measured at fair value through profit or loss.

In paragraph BC63 'except to adjust for consolidation procedures and for the effects of the business combination in which the parent acquired the subsidiary' is footnoted with the following text.

In October 2012 the Board issued *Investment Entities* (Amendments to IFRS 10, IFRS 12 and IAS 27), which amended paragraph D17 to clarify its application to investment entities, as defined in IFRS 10.

IFRS 3 *Business Combinations*

In paragraph BC24 'one or more other businesses' is footnoted with the following text.

In October 2012 the Board issued *Investment Entities* (Amendments to IFRS 10, IFRS 12 and IAS 27), which removed from the scope of IFRS 3 *Business Combinations* the acquisition by an investment entity, as defined in IFRS 10 *Consolidated Financial Statements*, of an investment in a subsidiary required to be measured at fair value through profit or loss.

In paragraph BC384 'operations of the acquiree' is footnoted with the following text.

In October 2012 the Board issued *Investment Entities* (Amendments to IFRS 10, IFRS 12 and IAS 27), which required investment entities, as defined in IFRS 10, to measure their investments in subsidiaries, other than those providing investment-related services or activities, at fair value through profit or loss.

IFRS 5 *Non-current Assets Held for Sale and Discontinued Operations*

The footnote to paragraph BC24B is amended. New text is underlined.

... The requirement to consolidate a subsidiary until control is lost did not change. <u>In October 2012 the Board issued *Investment Entities* (Amendments to IFRS 10, IFRS 12 and IAS 27), which required investment entities, as defined in IFRS 10 *Consolidated Financial Statements*, to measure their investments in subsidiaries, other than those providing investment-related services or activities, at fair value through profit or loss.</u>

IFRS 9 *Financial Instruments* (as issued in November 2009)

In paragraph BC86 'in accordance with IFRS 9' is footnoted with the following text.

In October 2012 the Board issued *Investment Entities* (Amendments to IFRS 10, IFRS 12 and IAS 27), which required investment entities, as defined in IFRS 10 *Consolidated Financial Statements*, to measure their investments in subsidiaries, other than those providing investment-related services or activities, at fair value through profit or loss.

IFRS 9 *Financial Instruments* (as issued in October 2010)

In paragraph BC5.25(a) 'in accordance with IFRS 9' is footnoted with the following text.

In October 2012 the Board issued *Investment Entities* (Amendments to IFRS 10, IFRS 12 and IAS 27), which required investment entities, as defined in IFRS 10 *Consolidated Financial Statements*, to measure their investments in subsidiaries, other than those providing investment-related services or activities, at fair value through profit or loss.

IFRS 13 *Fair Value Measurement*

Paragraph BC238(a) is footnoted with the following text.

In October 2012 the Board issued *Investment Entities* (Amendments to IFRS 10, IFRS 12 and IAS 27), which required investment entities, as defined in IFRS 10 *Consolidated Financial Statements*, to measure their investments in subsidiaries, other than those providing investment-related services or activities, at fair value through profit or loss. In their redeliberations on the Investment Entities project, the Board considered providing a net asset value practical expedient. However, the Board decided against this because there are different calculation methods in different jurisdictions and it is outside the scope of the Investment Entities project to provide fair value measurement guidance for investments in investment entities.

IAS 28 *Investments in Associates and Joint Ventures*

Paragraph BC9 is footnoted with the following text.

In October 2012 the Board issued *Investment Entities* (Amendments to IFRS 10, IFRS 12 and IAS 27), which required investment entities, as defined in IFRS 10 *Consolidated Financial Statements*, to measure their investments in subsidiaries, other than those providing investment-related services or activities, at fair value through profit or loss. The amendments did not introduce any new accounting requirements for investments in associates or joint ventures.

IAS 39 *Financial Instruments: Recognition and Measurement*

In paragraph BC24A 'paragraph 2(g) of IAS 39.' is footnoted with the following text.

In October 2012 the Board issued *Investment Entities* (Amendments to IFRS 10, IFRS 12 and IAS 27), which amended paragraph 2(g) to clarify that the exception should only apply to forward contracts that result in a business combination within the scope of IFRS 3 *Business Combinations*.

Amendments to the Basis for Conclusions on IFRS 12 *Disclosure of Interests in Other Entities*

Paragraph BC13 is footnoted with the following text.

Investment Entities (Amendments to IFRS 10, IFRS 12 and IAS 27), issued in October 2012, introduced an exception to the principle that all subsidiaries shall be consolidated. The amendments define an investment entity and require a parent that is an investment entity to measure its investments in particular subsidiaries at fair value through profit or loss instead of consolidating those subsidiaries. In addition, the amendments introduce new disclosure requirements related to investment entities in IFRS 12 *Disclosure of Interests in Other Entities* and IAS 27 *Separate Financial Statements*. The amendments are discussed in paragraphs BC215–BC317 of IFRS 10 *Consolidated Financial Statements*, and the disclosure requirements are discussed in paragraphs BC61A–BC61H of this IFRS.

After paragraph BC61, a heading and paragraphs BC61A–BC61H are added.

Investment entities

BC61A *Investment Entities* (Amendments to IFRS 10, IFRS 12 and IAS 27) introduced a requirement for investment entities to measure their investments in particular subsidiaries at fair value through profit or loss instead of consolidating them. The Board also decided on specific disclosure requirements for investment entities.

BC61B In deciding on the appropriate disclosure requirements for investment entities, the Board noted that investment entities would be required to make the disclosures already contained in other Standards. In particular, the disclosure requirements in IFRS 7 *Financial Instruments: Disclosures*, IFRS 13 *Fair Value Measurement* and IAS 24 *Related Party Disclosures* are likely to be relevant for users of investment entity financial statements.

BC61C Users told the Board that disclosures relating to the valuation methodology used for measuring fair value and the underlying inputs are essential to their analyses. This information is already required by IFRS 7 and by IFRS 13 when reporting investments at fair value through profit or loss or other comprehensive income in accordance with IFRS 9 *Financial Instruments* or IAS 39 *Financial Instruments: Recognition and Measurement*. Accordingly, the Board decided that it was not necessary to propose any additional disclosure requirements relating to the fair value measurements made by investment entities.

BC61D In the Exposure Draft *Investment Entities* (the *Investment Entities* ED), the Board proposed that an investment entity would be required to meet a disclosure objective that addressed all of an investment entity's investing activities. The *Investment Entities* ED also gave a number of examples of ways in which an investment entity could meet that disclosure objective. Respondents generally supported the disclosure guidance. However, the Board noted that it was outside the scope of the Investment Entities project to require all investment entities to provide disclosures about their investing activities. Consequently, the Board decided to remove the disclosure objective and the examples on how to meet the objective from the final requirements. Because the Investment Entities project focuses on providing an exception to consolidation, the Board decided to limit additional disclosures to information about unconsolidated subsidiaries.

BC61E The Board also decided to require an investment entity to disclose the fact that it has applied the exception to consolidation, noting that such a disclosure would represent useful information. Moreover, the Board decided to require an investment entity to disclose when it does not display one or more of the typical characteristics of an investment entity, along with a justification of why it still meets the definition of an investment entity.

BC61F The Board considered whether all of the disclosures in this IFRS should apply to the investments in unconsolidated subsidiaries, associates and joint ventures of investment entities. The Board decided that some (eg summarised financial information and information about non-controlling interests) are not applicable to investment entities and are inconsistent with the assertion that fair value information is the most relevant information for investment entities. Consequently, the Board decided to specify the IFRS 12 requirements applicable to the unconsolidated subsidiaries, associates and joint ventures held by investment entities.

BC61G Consistently with the principles in this IFRS, the Board decided to require an investment entity to disclose when any explicit or implicit financial support has been provided to entities that it controls. The Board concluded that it would help users of financial statements to understand an investment entity's exposure to risk.

BC61H The Board decided that an investment entity should disclose the nature and extent of any significant restrictions (eg resulting from borrowing arrangements or regulatory requirements) on the ability of investees to transfer funds to the investment entity in the form of cash dividends, or repayment of loans or advances. The Board considered this requirement to be useful for investors because such restrictions could potentially affect distributions to investors of the investment entity's returns from investments.

Amendments to the Basis for Conclusions on IAS 27 *Separate Financial Statements*

After paragraph BC8, a heading and paragraph BC8A are added.

Investment entities

BC8A *Investment Entities* (Amendments to IFRS 10, IFRS 12 and IAS 27), issued in October 2012, introduced an exception to the principle in IFRS 10 that all subsidiaries shall be consolidated. The amendments define an investment entity and require a parent that is an investment entity to measure its investments in particular subsidiaries at fair value through profit or loss in accordance with IFRS 9 *Financial Instruments* (or IAS 39 *Financial Instruments: Recognition and Measurement*, if IFRS 9 has not yet been adopted) instead of consolidating those subsidiaries. Consequently, the Board decided to amend IAS 27 to require an investment entity to also measure its investments in subsidiaries at fair value through profit or loss in its separate financial statements. The Board also made corresponding amendments to the disclosure requirements for an investment entity's separate financial statements, noting that if an investment entity prepares separate financial statements as its only financial statements, it is still appropriate for the investment entity to make the disclosures otherwise required in IFRS 12 about its interests in subsidiaries.

