ED 160 sub 5

Department of Treasury and Finance

The Treasury Building
21 Murray Street, HOBART, Tas 7000
GPO Box 147, HOBART, Tas 7001 Australia
Telephone: (03) 6233 3100 Facsimile: (03) 6223 2755
Email: secretary@treasury.tas.gov.au Web: www.treasury.tas.gov.au

Mr David Boymal
Chairman
Australian Accounting Standards Board
PO Box 204
COLLINS STREET WEST Vic 8007

Dear Mr ~~Boymal~~ David

EXPOSURE DRAFT 160 – COST OF AN INVESTMENT IN A SUBSIDIARY, JOINTLY CONTROLLED ENTITY OR ASSOCIATE

The Heads of Treasuries Accounting and Reporting Advisory Committee (HoTARAC) welcomes the opportunity to respond to the Australian Accounting Standards Board's Exposure Draft ED 160 *Cost of an Investment in a Subsidiary, Jointly Controlled Entity or Associate* (ED 160).

HoTARAC generally agrees with most of the changes proposed in the Exposure Draft, but a dissenting view is expressed in Question 4. HoTARAC does not agree with the proposed change in paragraph 37B of IAS 27 *Consolidated and Separate Financial Statements* and consequent amendments to other standards, as discussed in the following attachment.

If you have any queries regarding the above, please contact Sue Highland from Queensland Treasury on 07 3405 6064 or sue.highland@treasury.qld.gov.au.

Yours sincerely

D W Challen
SECRETARY

12 February 2008

Encl

Contact: Suzi Ransom
Phone: (03) 6233 2881
Our Ref: D/14481 SR/CJ

Exposure Draft ED 160
Cost of an Investment in a Subsidiary, Jointly Controlled Entity or Associate

General Comments

The proposed amendments to IFRS 1 within this ED will have little impact on the Australian public sector, as the majority of Australian public sector entities adopted the Australian Equivalents to International Financial Reporting Standards in 2005.

HoTARAC supports the proposed amendment to IAS 27, other than the paragraph 37B amendment. There are two differing viewpoints in relation to paragraph 37B. These are expressed below under Question 4, along with the HoTARAC rationale for not supporting this amendment.

Specific Comments

Question 1- Deemed cost
Do you agree with the two deemed cost options as they are described in this exposure draft? If not, why?

HoTARAC agrees with this proposal.

Question 2 – Changes in scope
Do you agree with the proposal to allow the deemed cost option for investments in jointly controlled entities and associates? If not, why?

HoTARAC agrees with this proposal.

Question 3 – Cost Method
Do you agree with the proposal to delete the definition of the cost method from IAS 27? If not, why?

HoTARAC agrees with this proposal.

Question 4 – Dividends as income and impairment testing
Do you agree with the proposed requirement for an investor to recognise as income dividends received from a subsidiary, jointly controlled entity or associate and the consequential requirement to test the related investment for impairment? If not, why?

A majority of HoTARAC members agree with the proposal for a dividend received from a subsidiary, jointly controlled entity or associate to be recognised as income to the extent that it is consistent with IAS 18 *Revenue* which describes dividends received as revenue as "...distributions of profits to holders of equity investments in proportion to their holdings of a particular class of capital".

However, HoTARAC does not agree with the consequential requirement to undertake impairment testing on receipt of a dividend. The receipt of a dividend does not always indicate a decrease in the value of the investment. The receipt of a

dividend often is an indicator of financial performance and not an indicator of financial position.

Dissenting View

Two HoTARAC members disagree with the proposal that dividends be recognised as income, irrespective of whether they are sourced from pre-acquisition or post-acquisition retained earnings. It is their view that:

Dividends as Income

> "The reasons for the change in the Basis for Conclusions are not persuasive. Paragraph BC 18 correctly notes that the principle underpinning the cost method is that a return of an investment should be deducted from the carrying amount of the investment. This is a fundamental principle, that a dividend is a return on an investment in contrast to a return of capital. From the perspective of the parent, dividends from pre-acquisition profits are a return of capital.
>
> According to paragraph BC 18 "the current wording in IAS 27 creates a problem in some jurisdictions because it makes specific reference to retained earnings as the means of making the assessment. The Board determined that the best way to resolve the issue was to delete the definition of the cost method". It is not clear from paragraph BC 18 why the reference to retained earnings is a "problem in some jurisdictions".
>
> A better solution is to preserve the IAS 27 paragraph 4 distinction between distributions from pre and post acquisition sources because it reflects a fundamental principle and, if necessary, address separately the effect of this paragraph in jurisdictions where it is a problem.

Impairment

> "However, if the distinction between distributions from pre and post acquisition sources is removed, we agree with the IASB's proposed impairment test requirement for investments in a subsidiary, jointly controlled entity or associate. As noted at paragraph BC 20, this proposed requirement is intended "to reduce the risk that removing the definition of the cost method will lead to investments in subsidiaries, jointly controlled entities and associates being systematically overstated in the separate financial statements of the investor". In short, whenever dividends exceed post-acquisitions of the subsidiary, which is come from pre-acquisition profits, the value of an investment recorded at cost has been impaired".

Question 5 – Formation of a new parent

Do you agree with the proposed requirement that in applying paragraph 37(A) of IAS 27, a new parent should measure cost using the carrying amounts of the existing entity? If not, why?

HoTARAC agrees with this proposal

Question 6 – Transition

HoTARAC agrees with this proposal