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28 November 2011

The Chairman
 Australian Accounting Standards Board
 PO Box 204
 Collins Street West
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Dear Sir/Madam

AASB Exposure Draft ED 220 Investment Entities

Industry Funds Management Pty Ltd (IFM), as a substantial provider of financial returns to over 5 million Australians, is pleased to respond to the AASB's ED 220 Investment Entities and to outline our support for the adoption of the ED 220 Investment Entities requirements in full.

IFM is an institutional fund manager that specialises in the management of investment products across four asset classes, namely Debt Investments, Listed Equities, Global Infrastructure and Global Private Equity.

IFM is owned by 32 major Australian superannuation funds, many of which are also our clients. This "no conflict" ownership structure aligns the interests of IFM's owners with its clients and allows us to focus on delivering superior long-term investment outcomes. To do this, we adopt a patient, strategic approach to investment management that considers environmental, social and governance factors.

IFM is headquartered in Melbourne and has teams based in Australia, Europe and North America. The firm's clients and investment professionals are located in three of the world's four largest pension markets. As at 31 October 2011, IFM manages A\$31.6 billion in global assets, on behalf of 60 clients representing over 5 million members of Australian and US Superannuation/Pension Funds.

Across our four asset classes we have one common valuation methodology, which is to provide fund Net Asset Valuations (NAV) at 'fair value', which is the basis for the unit pricing calculations we undertake on a daily or weekly basis, across all of our funds. The AASB's ED 220 Investment Entities paper discussion goes to the very heart of IFM's daily processes and the informational content of our annual accounts across a wide range of funds, geographies and legal ownership structures.

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 IFM Infrastructure Funds, ABN 91 157 945 930
 IFM International Private Equity Fund I, ABN 27 876 336 538
 IFM International Private Equity Funds, ABN 40 869 828 619
 IFM International Private Equity Fund III, ABN 21 393 445 075
 IFM Listed Equity Funds Pooled Superannuation Trust, ABN 51 088 318 274

IFM as the manager has no legal ownership in the underlying funds or assets, with Industry Funds Management (Nominees) Ltd acting as trustee to the various funds on behalf of the underlying investors, who have full beneficial entitlement to the underlying returns and net assets of the funds.

The particular asset class to which ED 220 is most relevant for IFM is our Infrastructure Funds. IFM currently manages assets of over A\$9.4b across Australian and International Infrastructure. Australian investors invest through a Pooled Superannuation Trust (PST), while our US and UK investors invest via Limited Partnerships into a Caymans registered Master Trust, which is also invested in by the Australian PST. The investments range from minority shareholdings in unlisted assets such as airports, toll roads, PPPs (aged care facilities, water utilities, schools, train stations) seaports and pipelines, up to 100% ownership in some cases. As our assets are unlisted, there are no market data services providing valuations, but IFM requires and sources quarterly independent valuations on every asset in which we invest, regardless of the ownership percentage.

The fair value of a long lived infrastructure asset is based on a discounted cash flow model, taking into account a myriad of market variables. This fair value will most definitely be different to the net book value of the investment entity, essentially reflecting the value to a willing buyer and a willing seller of those future cash flows in the context of a risk adjusted required return.

The sum of the portfolio investments at fair value form the net asset value of the fund, which in turn is the numerator for the valuation of an investor's individual unit or ownership interest in the fund. The investment industry expects unit prices to be available within hours of a period end, and our current timelines for weekly and monthly unit prices are by CoB next business day. This is possible because the valuation is a single point estimate sourced specific to that period. It is not, and it would be virtually impossible to be the sum of individual trail balances from a myriad of underlying operating entities in which we invest.

The concept of Consolidated Accounts is an important one in the context of groups of companies, parents and subsidiaries, but this is not the reality of the investment purpose. The IFM Infrastructure Fund is an amalgam of many disparate investment entities, with a wide range of ownership percentages, across a range of industries and geographies. The companies in which we invest are fully autonomous legal entities, running their own operations and Boards, and this is the same whether we own 5% or 100% of the asset. The operating entities prepare their own group accounts and are compliant with accounting standards that apply to them as separate legal corporate structures and this would not change under ED 220.

The point to note is that the IFM Infrastructure Fund, as an investment entity under all of the definitions proposed, would be unable to aggregate minority investment positions held at fair value with consolidated accounts for entities in which we have even obvious control of greater than 50%, and still get our a unit price by CoB next business day, as required by the investors we serve.

The final issue to highlight is the lack of informational value to investors in a pooled investment vehicle of consolidated accounts of disparate assets. For example, within the IFM Infrastructure Fund we would have a situation whereby we have majority ownership interests in airports and a renewable energy entity. In both cases the fair value of these assets to an investor is substantially higher than the net book value of the corporate entities, due to their future growth potential reflected in the forecast cash flows underlying their DCF valuations.

We note that the AASB issued ED 220 'Investment Entities' incorporating the IASB ED, however the introduction states that the AASB has "...significant concerns with the proposals in ED/2011/4, many of which are similar to the Alternative Views expressed by three IASB members...". IFM is a very keen supporter of truly global accounting standards. We currently provide financial reporting across three geographies, with investors in the US, UK and Australia. We find that the variation in accounting standards across these geographies creates additional cost in our business operations and we support the broader adoption of IFRS globally. In this regard, we strongly encourage the AASB to fully comply with the final IFRS standard once it is ratified.

Yours faithfully



Philip Dowman CA
Executive Director – Finance and Operations
Industry Funds Management Pty Ltd
Industry Funds Management (Nominees) Limited

SN	Question	Response and Comments
1	<p>Do you agree that there is a class of entities, commonly thought of as an investment entity in nature should not consolidate controlled entities and instead measure them at fair value through profit or loss? Why or why not?</p>	<p>We support the exception to consolidation because measuring an investment entity controlled investees at fair value results in information that is more decision-useful as it is better aligned with the entity's business model.</p> <p>IFM believes that it is preferable for an entity to consolidate another entity that it controls in the context of a Corporate Structure or Group of Companies. However, for investment entities, where the holding of a range of assets is on behalf of external investors, the consolidation of disparate operating companies provides limited if any informational value.</p> <p>Typically, fair values of the net assets of the investment entity are established frequently as fair value is the basis on which investors make their decisions on whether to hold or put their investment back for cash.</p> <p>Investment entities often hold varying ownership positions in an entity although their investment strategy may be the same for each entity, regardless of the ownership proportions held. The objective of an investment, to maximize its return on investment through capital appreciation, dividends or interest, is the same regardless of the percentage ownership interest that is held in an investee. Therefore, it would be reasonable to apply a similar accounting treatment to both investments, regardless of ownership interest, as the economics and management's intent are effectively the same.</p> <p>The concept of whether there are exceptions to general principles because fair value is more relevant is not unique to controlled investments of investment entities. The IASB has in the past acknowledged in IAS 28 its view that equity or proportionate consolidation methods of accounting for investments held by venture capital organizations, mutual funds, unit trusts and similar entities often produces information that is not relevant to their management and investors and that fair value measurement produces more relevant information.</p>
2	<p>Do you agree that the criteria in this exposure draft are appropriate to identify entities that should be required to measure their investments in controlled entities at fair value through profit or loss? If not, what alternative criteria would you propose, and why are those criteria more appropriate?</p>	<p>We agree with the criteria for determining whether an entity is an investment entity.</p> <p>We are, in general, not in favour of options that offer entities a free choice between alternative accounting treatments. In addition, we believe that consolidated financial statements provide the most useful form of financial reporting for most types of entities. Therefore, we agree that it is necessary to limit the use of the investment entity exception to those entities for which consolidated financial information would be less decision useful than measurement at fair value.</p> <p>We agree with all of the criteria that an entity must meet to qualify as an investment entity.</p>

SN	Question	Response and Comments
3	<p>Should an entity still be eligible to qualify as an investment entity if it provides (or holds an investment in an entity that provides) services that relate to:</p> <p>a) Its own investment activities? b) The investment activities of entities other than the reporting entity?</p> <p>Why or why not?</p>	<p>We believe that if an investment entity provides investment services to its own investment business then this should not affect the investment entity classification.</p> <p>We believe that accounting by investment entities should reflect the underlying substance of their business. Therefore, we agree that an investment entity should consolidate all activities related to the management of their portfolio regardless of whether they are carried out by the entity itself or a subsidiary.</p> <p>We agree with the criterion in paragraph 2(a) of the ED, which requires that an investment entity's only substantive activities are investing in multiple investments. Consequently, we believe that an entity that operates a significant business that provides services to entities outside its group would not be an investment entity.</p>
4	<p>a) Do you agree that it is appropriate to use this disclosure objective for investment entities rather than including additional specific disclosure requirements? b) Do you agree with the proposed application guidance on information that could satisfy the disclosure objective? If not, why not and what would you propose instead?</p>	<p>There are no conceptual reasons why an investment entity that has a single investor could not be an investment entity. However, we appreciate the difficulty that could exist in practice to distinguish between a 'true' investment entity and entities that are set up for other purposes. We believe that an 'investment-type' entity that engages in transactions with other members of their parent's group on terms that are possibly not arm's length should not be eligible for the investment entity exception, because such entity obtains benefits that are not capital appreciation and/or investment income in nature.</p>
5	<p>Do you agree that investment entities that hold investment properties should be required to apply the fair value model in IAS 40, and do you agree that the measurement guidance otherwise proposed in the exposure draft need apply to financial assets, as defined in IFRS 9 and IAS 39 Financial Instruments: Recognition and Measurement? Why or why not?</p>	<p>We agree that an investment entity that manages substantially all of its investments at fair value should measure investment properties and financial assets at fair value.</p> <p>A key characteristic of an investment entity is that it manages substantially all of its investments at fair value (paragraph 2(e) of the ED). Accordingly, we agree that if this is the case that an investment entity should also apply fair value measurement to asset classes such as investment property and financial assets, to the extent that they are managed with the same purpose and on a fair value basis as well.</p>

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6	<p>Do you agree that the parent of an investment entity that is not itself an investment entity should be required to consolidate all of its controlled entities including those it holds through subsidiaries that are investment entities? If not, why not and how would you propose to address the Board's concerns?</p>	<p>We are not in favour of requiring that a parent, which is not an investment entity itself, to consolidate the controlled entities that it holds through subsidiaries that are investment entities.</p> <p>In our view, if application of the investment entity exception at the subsidiary level results in fair value information that is more decision-useful than consolidated information then – absent important intercompany transactions and relationships – we would expect such fair value information to be relevant in the financial statements of the ultimate parent entity. In addition, the frequent acquisitions and disposals of businesses by an investment entity subsidiary would lead to consolidation of investees for relatively short periods and would affect the decision-usefulness of the consolidated financial statements of the parent.</p> <p>The Board's decision not to allow a non-investment entity parent to retain the accounting of its investment entity subsidiaries was motivated by concerns about potential accounting inconsistencies and possibilities for abuse.</p> <p>a) We understand the complications and potential accounting inconsistencies that might arise if a subsidiary that is an investment entity were to hold an equity interest in the ultimate parent or invest in the same investees as the parent. However, we believe that those concerns would be better addressed by modifying the investment entity criteria (e.g. requiring that an investment entity not make such investments) or prescribing the accounting to be applied if such investments did exist (e.g. application of some form of consolidation accounting to those investments).</p> <p>b) We do not share the concerns regarding the possibilities for abuse and the potential for off-balance sheet accounting for some assets because:</p> <ol style="list-style-type: none"> i. The criteria in paragraph 2 of the ED, in particular the need for unrelated external investors, prevent entities that are not in substance investment entities from qualifying for the use of the consolidation exception. In other words, only entities that are investment entities in their own right qualify for the exception; and ii. The conditions set in paragraph B6 of the ED ensure that the parent cannot obtain benefits other than those from capital appreciation and/or investment income from investees held by an investment entity subsidiary. Consequently, any arrangement between the parent and its investment entity subsidiary that modifies the nature of the investment activity would disqualify the entity from using the consolidation exception.

SN	Question	Response and Comments
7	<p>a) Do you agree that it is appropriate to use this disclosure objective for investment entities rather than including additional specific disclosure requirements?</p> <p>b) Do you agree with the proposed application guidance on information that could satisfy the disclosure objective? If not, why not and what would you propose instead?</p>	<p>We agree with the disclosure objective as stated. However, we are concerned about the level of detailed narrative that has been included to explain the objective:</p> <p>a) While the disclosures suggested in paragraph B19 of the ED might be helpful to users of the financial statements, it is unclear how exactly the IASB selected these particular suggested disclosures. In addition, given that such lists of examples are often interpreted as being requirements, we would be in favour of a shorter, more targeted list.</p> <p>b) Paragraph B20 of the ED places the onus on the preparer to decide which disclosures in IFRS 7, IFRS 12, IFRS 13 and the disclosure proposals of the ED result in duplication. We believe that it would be more efficient if the IASB, as a standard setter, would carry out this task rather than multiplying the effort by requiring each and every investment entity to do this.</p>
8	<p>Do you agree with applying the proposals prospectively and the related proposed transition requirements? If not, why not? What transition requirements would you propose instead and why?</p>	<p>We believe that the requirements should be applied retrospectively, unless impracticable. This would avoid inconsistencies with the transitional provisions of IFRS 10 and result in information that is more comparable.</p> <p>We believe that the transition requirements should be consistent with the transitional requirements in IFRS 10 Consolidated Financial Statements. That is, if a parent entity no longer consolidates an investee because it meets the criteria of an investment entity it shall apply the requirements retrospectively in accordance with IAS 8 Accounting Policies, Changes in Accounting Estimates and Errors unless that is impracticable.</p> <p>The proposals for prospective application would result in serious issues regarding the comparability of the current period and the comparative period(s). That is, in the first year of application of the standard, an investment entity would measure its controlled investees at fair value whilst in the comparative period it would consolidate the underlying net assets of its controlled investees. This, in our view, would seriously impair the usefulness of the financial statements in the year in which these proposals are first adopted.</p> <p>We understand that the Board is concerned about the undue use of hindsight in determining the fair value of investees. However, to qualify for the use of the exception, an investment entity must manage its investments at fair value. Therefore, we believe that investment entities would have collected fair value information contemporaneously and that the risks associated with use of hindsight are limited. Entities that did not meet the investment entity criteria in earlier periods would only be permitted to use the exception prospectively from the date on which they meet those criteria.</p>

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9	<p>a) Do you agree that IAS 28 should be amended so that the mandatory measurement exemption would apply only to investment entities as defined in the exposure draft? If not, why not?</p> <p>b) As an alternative, would you agree with an amendment to IAS 28 that would make the measurement exemption mandatory for investment entities as defined in the exposure draft and voluntary for other venture capital organisations, mutual funds, unit trusts and similar entities, including investment-linked insurance funds? Why or why not?</p>	<p>We agree that IAS 28 should be amended to be consistent with the use of the investment entities definitions.</p>