



5 January 2012

International Accounting Standards Board  
1<sup>st</sup> Floor 30 Cannon Street  
London EC4M 6XH  
United Kingdom

*(By online submission)*

Dear Sirs

## **RESPONSE TO EXPOSURE DRAFT ON INVESTMENT ENTITIES**

The Singapore Accounting Standards Council appreciates the opportunity to comment on the Exposure Draft on Investment Entities (the ED) issued by the International Accounting Standards Board (the Board) in August 2011.

Overall, we are supportive of the Board's proposal to provide an exception to consolidation for investees controlled by an investment entity on the basis that the measurement of these investments at fair value would enhance the decision usefulness of the financial statements of investment entities.

However, we do not agree that the non-investment entity parent of an investment entity should be required to consolidate controlled investees held via the investment entity. We are of the view that if it is considered that consolidation at the investment entity level does not provide decision-useful information to users, it is difficult to conceive that consolidation at the parent level would do so.

Furthermore, whilst we broadly agree with the criteria for determining whether an entity is an investment entity, we believe that a key feature of an investment entity is the existence of exit strategies for investments held for purposes of capital appreciation. Accordingly, we recommend that the Board explicitly incorporate it within the criteria so as to enhance the distinction between a genuine investment entity and an operating conglomerate.

Our comments on the specific questions in the ED are as follows:

## **Question 1— Exclusion of investment entities from consolidation**

**Do you agree that there is a class of entities, commonly thought of as an investment entity in nature, that should not consolidate controlled entities and instead measure them at fair value through profit and loss? Why and why not?**

We support the Board's proposal to provide an exception to consolidation for investees controlled by investment entities. We agree that such entities should measure controlled investees at fair value through profit and loss as this would better align financial reporting with the entities' business model, thereby resulting in more relevant and decision-useful financial information. We consider that reporting controlling and non-controlling interests on a different basis (i.e. consolidation and fair value respectively) would impede comparability within the financial statements of an investment entity given that these investments are held by the investment entity for one sole objective, which is that of capital appreciation and/or investment income.

## **Question 2—Criteria for determining when an entity is an investment entity**

**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?**

We generally agree with the criteria set out in the ED.

However, we are of the view that a key feature of an investment entity is the existence of exit strategies for investments held for purposes of capital appreciation, particularly in the case of an investment entity that "actively" manages its controlled investees. As such, we recommend that the Board explicitly incorporate this requirement as one of the criteria for investment entities within paragraph 2 of the ED as this would help to distinguish a genuine investment entity from an operating conglomerate.

In respect of the criterion on "pooling of funds", we do not agree with paragraph B16 of the ED that an entity with a single investor must be formed "in conjunction" with the formation of the single investor that is itself an investment entity in order for the entity to qualify as an investment entity. We consider that as long as there is pooling of funds at a higher level in the investment structure, the timing of formation of the entities should be irrelevant. We recommend that the Board clarify the rationale for the requirement in paragraph B16 and/or to modify the requirement in paragraph B16 accordingly.

### Question 3—Nature of the investment activity

**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:**

**(a) its own investment activities?**

**(b) the investment activities of entities other than the reporting entity?**

**Why and why not?**

We are of the view that an entity that provides services that relate to its own investment activities either directly or indirectly through an investee should still be eligible to qualify as an investment entity.

In respect of an entity that provides services that relate to the investment activities of other entities, we believe that the entity should qualify as an investment entity provided the provision of such services is not substantive.

### Question 4— Pooling of funds

**(a) Should an entity with a single investor unrelated to the fund manager be eligible to qualify as an investment entity? Why or why not?**

**(b) If yes, please describe any structures/examples that in your view should meet this criterion and how you would propose to address the concerns raised by the Board in paragraph BC16.**

Whilst we believe there are no conceptual reasons why a single investor entity could not be an investment entity, we agree with the Board that the “pooling of funds” criterion is a necessary feature to minimise any form of potential abuse.

### Question 5—Measurement guidance

**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 only to financial assets, as defined in IFRS 9 and IAS 39: *Financial Instruments: Recognition and Measurement*? Why or why not?**

We agree that investment entities that hold investment properties should be required to apply the fair value model in IAS 40 as this is consistent with the nature of an investment entity. However, we believe that the proposed measurement guidance should not be restricted only to financial assets as investment entities may invest in non-financial assets such as wine or art pieces for capital appreciation.

**Question 6—Accounting in the consolidated financial statements of a non-investment entity parent**

**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?**

We disagree that the non-investment entity parent of an investment entity should be required to consolidate controlled investees held via the investment entity. To this end, we support the Financial Accounting Standards Board (FASB)’s Exposure Draft on Investment Companies which requires a non-investment entity parent to retain the accounting applied by its investment entity subsidiaries in its consolidated financial statements.

We consider that the accounting treatment, whether at the subsidiary or parent level, should be driven primarily by the decision-usefulness of information presented to users. If it is argued that consolidation at the investment entity subsidiary level does not provide decision-useful information, we are not persuaded that consolidation at the parent level would do so. We note that this fact was also acknowledged by the Board in paragraph BC20 of the Basis for Conclusion.

In addition, given the nature of investment entities, acquisition and disposal of investments, including controlled investees, are likely to be fairly frequent. This gives rise to frequent consolidation and deconsolidation of controlled investees by the non-investment entity parent which would impair the decision-usefulness of the parent’s consolidated financial statements.

Furthermore, we observe that the proposal for the non-investment entity parent of an investment entity to consolidate controlled investees held via the investment entity contradicts another proposal in the ED which requires the non-investment entity parent to retain the fair value accounting applied by its investment entity subsidiary to associates and joint ventures in its consolidated financial statements and we question the rationale for the inconsistent treatment.

We understand that the proposal was driven by the Board’s concerns of the potential accounting inconsistencies and possibilities for abuse as highlighted in paragraph BC20. However, we believe these concerns would be better addressed by prescribing specific accounting guidance or by refining the investment entity criteria. Additionally, we are of the view that paragraphs 2(d) (which requires an investment entity to have investors that are unrelated to the parent) and B6 (which would prevent a parent from obtaining benefits other than investment income and/or capital appreciation) of the ED would mitigate the potential for abuse.

As such, we urge the Board to extend the consolidation exception to non-investment entity parents.

## Question 7—Disclosure

- (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?**

We are broadly supportive of the proposed disclosure objective.

However, we believe that the ED should clearly set out the disclosure requirements applicable to investment entities. We consider that it is not adequate to leave it to preparers to determine which disclosure requirements in IFRS 7, IFRS 12, IFRS 13 and the ED would result in unnecessary duplication, as indicated in paragraph B20 of the ED.

In addition, we are concerned that the long list of “examples” of additional disclosures in paragraph B19 of the ED may be perceived by constituents as mandatory disclosures. As such, we recommend that the Board streamline this list to include only examples of disclosures that are likely to be most useful to users.

## Question 8—Transition

**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?**

We are of the view that the proposals should be applied retrospectively in accordance with IAS 8. This would enhance the comparability and usefulness of the financial statements presented. In this regard, we do not share the Board’s concern on the use of hindsight in determining the fair value of the investments since to qualify as an investment entity, an entity must necessarily manage its investments on a fair value basis in the first place (i.e. fair value information would be available).

## Question 9—Scope exclusion in IAS 28 (as amended in 2011)

- (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?
- (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?

Whilst we can appreciate that the proposed amendment to IAS 28 would improve consistency within IFRSs, we question if it would result in decision-useful information for venture capital organisations, mutual funds, unit trusts and similar entities including investment-linked insurance funds that do not qualify as investment entities under the ED. We urge the Board to carry out further outreach to ascertain the implications of the proposed amendment.

### Other comment

We are concerned that the proposals in the ED could result in accounting for the form rather than the substance of some entities that hold investments via special purpose vehicles.

For example, a real estate investment trust (the trust) may hold investment properties (IPs) either directly or indirectly via special purpose vehicles (SPVs) for tax, legal, regulatory or other business reasons. In situations where SPVs are set up for the sole purpose of holding the IPs, the trust could be deemed not to meet the investment entity definition by virtue of the fact that the SPVs are not managed on a fair value basis since only the IPs held by the SPVs are managed on such a basis by the trust (the rest of the SPVs' assets and liabilities, e.g. bank loans obtained by the SPVs to finance the acquisition of the IPs, are not managed on a fair value basis by the trust). Conversely, if the trust holds the IPs directly, it would meet the investment entity definition.

As the SPVs are shelf conduits, we are of the view that: (1) the structure of the trust is not relevant to the assessment of whether the trust meets the investment entity definition given that the fundamental objective of the trust, regardless of its structure, is to invest in the underlying IPs for investment income and/or capital appreciation; and (2) the trust should account for the assets, liabilities, revenue and expenses of the SPVs on a line-by-line basis rather than measure the SPVs at fair value. This would better reflect the underlying economic substance, rather than the form, of the trust.

Accordingly, we urge the Board to refine the ED proposals to ensure that they do not result in accounting for the form, rather than the substance, of entities that hold investments via special purpose vehicles such as real estate investment trusts.

We hope that our comments will contribute to the Boards' deliberation on this ED. Should you require any further clarification, please contact the project manager Ee Wen Kuah at [Kuah Ee Wen@acra.gov.sg](mailto:Kuah_Ee_Wen@acra.gov.sg).

Yours faithfully

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Secretary  
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