

December 14, 2011

Via website posting: <http://www.iasb.org/>

Re: Exposure Draft: **Investment Entities (ED/2011/4)**

Dear Sir/Madam:

The Certified General Accountants Association of Canada (CGA-Canada) welcomes the opportunity to comment on the Exposure Draft: **Investment Entities (ED/2011/4)**. We have also provided additional comments on certain related matters.

Question 1

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 or loss? Why or why not?

Comment:

We are in general agreement with the proposed exception to consolidation because we believe that:

- measurement of investment entity controlled investees at fair value will result in more decision-useful information from the perspective of investors in the investment entity; and,
- proposed exception will facilitate presentation of the investment entity's business model more faithfully.

We suggest, however, that the proposed exception should be applied at the individual investment level, and not at the entity level. We believe that, even for non-investment entities, it would be appropriate to account for an investment at fair value through profit or loss, if such investment is intended to be held for earning income and/or capital appreciation, rather than for securing permanent control for the purpose of directing the investee's operating, financing and investing policies. We believe that application of the proposed exception, independently and objectively, at the individual investment level is conceptually more refined, since such application also considers the intent of the entity, and does not differentiate between investment and non-investment entities. Accordingly, the definition of control in IFRS 10 *Consolidated Financial Statements* should incorporate the concepts of both the ability to control and the intent to control. The intent of the entity can be evaluated on the basis of whether the investment is a passive portfolio investment or a long term strategic deployment of capital meant to serve a business purpose. If the proposed exception is applied at the individual investment level for all the entities, there will be no need to determine the eligibility of an entity to apply such exception.

We have commented on the other questions in this exposure draft without prejudice to what is stated above and assuming that the proposed exception is to be applied at the qualifying investment entity level.

Question 2

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?

Comment:

We generally agree with the criteria for determining whether an entity is an investment entity. However, we suggest inclusion of the following additional criterion for the purpose of determining eligibility of an entity to avail the proposed exception.

“The entity is recognized and governed in its jurisdiction by the laws and regulations applicable to an investment entity”.

We believe that such requirement will account for the differences in the business structures and business models prevailing in different jurisdictions. Also, it would be better to include documented exit strategy for an investment as a part of the eligibility requirements (Paragraph 2), instead of an application guidance (Paragraph B9).

Question 3

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 or why not?

Comment:

(a) We believe that, if an investment entity provides investment services to its own investment business, then its eligibility to apply the proposed exception should not be impacted because provision of such service can be considered a legitimate business of an investment entity, and accordingly we consider application guidance provided in the Paragraphs B2 and B3 as reasonable.

(b) We believe that if the aforementioned services are provided to the investment activities other than the reporting entity, the entity should be eligible to be classified as an investment entity, as long as the substantive activities of the entity continues to be investing in multiple investments. In such a case, we do not see any conceptual basis for making such distinction.

Question 4

(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.

Comment:

We believe that an investment entity with a single investor unrelated to the fund manager should not be

eligible to qualify as an investment entity because the absence of such a requirement would provide a parent company structuring opportunity for holding off-balance-sheet assets through an entity which is not a true investment entity, but only a conduit for the purpose of holding off-balance-sheet assets. We agree with the rationale provided in BC16.

Question 5

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?

Comment:

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 in conformity with the eligibility requirement articulated in the Paragraph 2(e). The fair value measurement of financial assets and investment properties in accordance with the provisions of IFRS 9 and IAS 40, respectively, will achieve consistency without making unwarranted distinction among the asset classes.

Question 6

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?

Comment:

We are not in favour of requiring that a parent, which is not an investment entity itself, consolidate the controlled entities that it holds through subsidiaries that are investment entities. We believe that more decision-useful information will be provided if the non-investment parent entity presents such controlled entities at fair value through profit or loss. We also believe that the possibilities of abuse and structuring for off-balance-sheet accounting are remote because of the provision in Paragraph 2(d) and the explicit application guidance articulated in Paragraph B6. We believe that any such apprehension can be better addressed by incorporating necessary safeguards in the eligibility requirements specified in Paragraph 2 of the proposal, rather than withdrawing the proposed exception for the non-investment parent entity in Paragraph 8 of the proposal.

Question 7

(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?

Comment:

(a) We agree with the conceptual basis of the disclosure objective as stated. However, for achieving consistency and comparability, it would be better to provide application guidance in the ED itself as to which disclosures in IFRS 7, 12 and 13 satisfy the disclosure requirements in the ED, and hence need not be duplicated. We are concerned that in the present ED, this task is entrusted to the preparers of the financial statements which may result in inefficiency as well as diversity in practice.

- (b) We are concerned that the examples of detailed disclosures specified in the Paragraph B19 could be misinterpreted as requirements, and may not be appropriate in all cases. We suggest including a clarification to the effect that the incremental costs of providing such disclosures should be weighed against incremental benefits resulting from such disclosures.

Question 8

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?

Comment:

We note the misalignment of the effective date in the present ED (prospective application) and the effective date in IFRS 10 (retrospective application). This would result in inconsistent accounting, and make the financial statements incomparable in the first year of application of the proposed exception. Hence, we believe that the requirements in the present ED should be applied retrospectively, unless impracticable. This would reduce inconsistencies with the transitional provisions of IFRS10 and result in information that is more comparable. We agree with the other transition requirements of the present ED.

Question 9

- (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?*

Comment:

- (a) We do not agree with the proposed amendments to IAS 28, but consider the alternative (b) discussed below to be more desirable. This is because we are not aware of any evidence-based rebuttal of the rationale in the original IAS 28 that justifies granting the irrevocable option of fair value accounting through profit or loss to the non-investment entities such as mutual funds, unit trusts and other venture capital organizations.
- (b) We consider this alternative to be more desirable than that discussed above as it promotes greater consistency and comparability among entities applying guidance in this ED. However, more detailed research and analysis may be necessary for better understanding of the impact of the proposed amendments to IAS 28.

Additional Comments

We have noted the concerns and reservations expressed by the dissenting Board members in their alternative views. We note that these concerns and reservations stem from the perceived misalignment of the proposals in the ED and the Conceptual Framework which is still under development. Hence, it is extremely important to accord the highest priority to the development of Conceptual Framework and to clarify its status in the hierarchy of IFRSs. We consider a robust Conceptual Framework *sine qua non* for effective and efficient development of high quality and internationally accepted financial reporting standards.

Should you wish to discuss the contents of this comment paper or require further elaboration on any of the items presented herein, please do not hesitate to contact Kamallesh Gosalia at kgosalia@cga-canada.org or alternatively the undersigned at rlefebvre@cga-canada.org.

Sincerely,

[Original signed by:]

Rock Lefebvre, MBA, CFE, FCIS, FCGA
Vice-President, Research & Standards