

Please note that the comments expressed herein are solely my personal views

Financial Accounting Standards Board
401 Merritt 7
PO Box 5116
Norwalk, CT 06856-5116
www.fasb.org

Chris Barnard
Germany

18 November 2011

- **File Reference No. 2011-200**
- **Financial Services – Investment Companies (Topic 946)**
- **Amendments to the Scope, Measurement, and Disclosure Requirements**

Dear Sir,

Thank you for giving us the opportunity to comment on your Exposure Draft: Financial Services – Investment Companies (Topic 946); Amendments to the Scope, Measurement, and Disclosure Requirements.

I will make some general comments here. The enclosed appendix contains the comment letter, which I submitted to the IASB on their exposure draft ED/2011/4: Investment Entities. This covers most of the remaining issues in more detail.

Convergence between FASB and IASB

In general I support these principles-based proposals, which will clarify the scope, measurement, presentation and disclosure requirements for investment companies. The proposals are clear and understandable, and they will improve convergence with IFRS, although some gaps would still remain. I support the proposal that an entity that is regulated as an investment company under the Securities and Exchange Commission's Investment Company Act of 1940 would be an investment company. This is reasonable, proportionate and appropriate. However, I do not agree with the proposal that an investment company should consolidate a controlling financial interest in another investment company in a fund-of-funds structure. In this case I prefer the IASB's proposal under which such an investment company would account for a controlling financial interest in another investment company at fair value, which is more in line with its business rationale. I must say that I also agree with the alternative view of Mr. Smith that is presented in BC53 – BC55.

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I would generally recommend that the FASB and the IASB should work much more closely together in order to develop a more unified standard for investment companies, in line with their commitments.

Yours faithfully

Chris Barnard

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APPENDIX

International Accounting Standards Board
30 Cannon Street
London EC4M 6XH
United Kingdom
www.ifrs.org

Chris Barnard
Germany

08 September 2011

- **Your Ref: Comment letter on Exposure Draft ED/2011/4**
- **Investment Entities**

Dear Sir,

Thank you for giving us the opportunity to comment on your exposure draft ED/2011/4: Investment Entities.

I agree with the proposals, which are clear, internally consistent and principles-based, and would align IFRSs more closely with US Gaap. The proposals would require an investment entity, as defined, to measure and report its investments in controlled entities at fair value through profit or loss in accordance with IFRS 9, rather than consolidating such investments. The proposals further require the investment entity to provide additional disclosures such that users of financial statements (users) could evaluate the nature and financial effect of its investment activities. This will align internal performance measurement with external financial reporting. I think that this is crucial, and I appreciate that the IASB is responding to investors' and other users' legitimate concerns here.

I agree with the proposed criteria for determining whether an entity is an investment entity, particularly the basic criterion that: "the purpose of the entity is investing to earn capital appreciation, investment income (such as dividends or interest), or both",¹ and the criteria concerning unitisation of investments, ownership, internal management and performance measurement. In such cases it is certainly more appropriate to look through the investment entity to the actual investments held, in order to promote internal consistency and provide more meaningful information to users.

¹ Paragraph 2(b), Exposure Draft.

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I do accept the concerns and alternative views that are presented in paragraphs AV1-14. However, given users' primary objections and stated requirements, I do not wholly agree with paragraph AV1 which state that "the proposal would result in the presentation of financial statements by investment entities that are less relevant and less representationally faithful than would be the case if controlled investees were consolidated". I would however prefer to minimise exceptions, particularly exceptions to the basic accounting requirements, such as consolidation.² In this vain I agree with paragraph AV5 that a useful compromise would be for the investment entity to consolidate investments in controlled entities and either disclose the fair value information in the notes to the financial statements or provide separate financial statements for the parent entity showing all investments in controlled entities at fair value, and disclose such additional information that would allow users to evaluate the nature and financial effect of its investment activities.

² I generally agree with paragraph AV10 that: "financial reporting requirements should be principle-based and contain few, if any, exceptions".

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Answers to specific questions raised by the IASB

Exclusion of investment entities from consolidation

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?

Yes. I broadly agree with this. The critical point is that investors and other users should be able to easily access the appropriate fair value information and relevant disclosures, including aggregate and per-unit disclosures, for qualifying investment entities. This would provide more meaningful information to users compared with just consolidating the controlled entities.

Criteria for determining when an entity is an investment entity (paragraphs 2 and B1–B17)

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?

Yes, the criteria in the ED are sufficient and complete in order to identify entities that should be required to measure their investments in controlled entities at fair value through profit or loss.

'Nature of the investment activity' (paragraphs 2(a) and B1–B6)

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?

I agree that an entity should still be eligible to qualify as an investment entity only if it provides (or holds an investment in an entity that provides) services that relate to its own investment activities. This is consistent with the requirement that the entity's only substantive activities are investing in multiple investments for capital appreciation, investment income, or both, and the intention that the entity should not obtain benefits from subsidiaries that would be unavailable to other investors.

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'Pooling of funds' (paragraphs 2(d) and B14–B16)

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.

Yes. This is not a problem given that investors unrelated to the entity or its affiliates should collectively have significant ownership in the investment entity.

Measurement guidance (paragraphs 6 and 7)

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?

Yes, this is consistent with the business and activities of an investment entity, and with the purpose of the ED.

Accounting in the consolidated financial statements of a non-investment entity parent (paragraph 8)

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?

Yes, I agree with the conclusions of paragraph BC20. This is a reasonable compromise.

Disclosure (paragraphs 9 and 10)

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?

Yes, I agree that an investment entity should provide information to enable users to evaluate the nature and financial effect of its investment activities. The information should be provided in aggregate and per-unit.

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(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?

The proposed application guidance is reasonable, but not complete. For example I would specifically recommend that you should include guidance relating to the different components of master-feeder structures.

Transition (paragraph C2)

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?

Yes, this is appropriate. I notice that paragraphs 5 and C2 refer to “accumulated other comprehensive income”. This term is not explicitly defined in IFRSs. Please would you clarify its definition here?

Scope exclusion in IAS 28 (as amended in 2011)

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?

I 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. This is transparent and would provide more consistency in financial reporting within IFRSs.

Yours faithfully

Chris Barnard