

Hans Hoogervorst
Chairman
International Accounting Standards Board
30 Cannon Street
London
United Kingdom
EC4M 6XH

15 September 2014

Dear Mr Hoogervorst

Exposure Draft ED/2014/2 – Investment Entities: Applying the Consolidation Exception

Deloitte Touche Tohmatsu Limited is pleased to respond to the International Accounting Standards Board's (the IASB's) Exposure Draft *Investment Entities: Applying the Consolidation Exception* ('the exposure draft').

We are concerned that in respect of two of the three areas addressed the proposals result in arrangements being differentiated on a basis other than the relevance of the resulting information. Specifically:

- we believe that the proposals to subsume a service providing entity into a single fair value number will, for some arrangements, result in an inappropriate lack of transparency and that they will allow structuring opportunities. For these reasons, we recommend that the Board consider a more principles-based approach to determining the appropriate accounting for different arrangements in which investment related services are provided by a subsidiary that is itself an investment entity; and
- an assumed difference in the ease of obtaining information is not sufficient reason to introduce a difference in the equity method of accounting for associates and joint ventures. As the equity method of accounting can validly be viewed as a valuation technique, we believe that retaining fair value measurement in applying this method to both associates and joint ventures that are investment entities would be appropriate.

Our detailed responses to the questions in the invitation to comment are included in the Appendix to this letter.

If you have any questions concerning our comments, please contact Veronica Poole in London at +44 (0) 20 7007 0884.

Yours sincerely

A handwritten signature in black ink, appearing to read 'V. Poole', is positioned above the printed name.

Veronica Poole
Global IFRS Leader

Appendix

Question 1 – Exemption from preparing consolidated financial statements

The IASB proposes to amend IFRS 10 to confirm that the exemption from preparing consolidated financial statements set out in paragraph 4(a) of IFRS 10 continues to be available to a parent entity that is a subsidiary of an investment entity, even when the investment entity measures its subsidiaries at fair value in accordance with paragraph 31 of IFRS 10. Do you agree with the proposed amendment? Why or why not?

We agree with the proposed amendment on cost/benefit grounds.

Question 2 – A subsidiary that provides services that relate to the parent's investment activities

The IASB proposes to amend IFRS 10 to clarify the limited situations in which paragraph 32 applies. The IASB proposes that the requirement for an investment entity to consolidate a subsidiary, instead of measuring it at fair value, applies only to those subsidiaries that act as an extension of the operations of the investment entity parent, and do not themselves qualify as investment entities. The main purpose of such a subsidiary is to provide support services that relate to the investment entity's investment activities (which may include providing investment-related services to third parties). Do you agree with the proposed amendment? Why or why not?

We have significant concerns that, whilst the proposed amendment will result in an appropriate outcome in some cases (for example, a 'fund of funds' arrangement), in other cases (including infrastructure funds and many private equity arrangements) the proposed amendment will result in an inappropriate lack of transparency as significant levels of activity relating to the group's investment related services will be subsumed into a single fair value number, thus obscuring movements in the fair value of the underlying investments that are managed on a fair value basis. Similarly, service entities that are themselves investment entities may hold gearing used to fund the investment portfolio and receive cash on disposal of investments that is then remitted to the parent investment entity. These balances would also be subsumed into the single fair value of the service entity and its investments, reducing the level of transparency on the funding of, and cash generated by, investments that are managed on a fair value basis.

The proposed amendment will also allow structuring opportunities as it will result in very different financial statements for the parent investment entity depending solely on whether services are provided by an entity that is also an intermediate holding company that is itself an investment entity, meaning that consolidation of an entity providing substantially all of a group's investment related services can be avoided simply by housing those activities in an investment entity. We do not believe that legal structuring, in itself, should be used to determine which information is most relevant to users.

For these reasons, we believe that before finalising any amendment the Board should consider a more principles-based approach to determining whether an entity would more appropriately be measured at fair value (according to the proposed amendment) or by accounting for each line item using uniform accounting policies, which would include measuring the subsidiary's investments in controlled investees at fair value (following the alternative approach referred to in paragraph BC8 of the Basis for Conclusions on the exposure draft). We believe that such an approach should be based on the business purpose of the entity, supported by indicators such as the key metrics communicated to investors.

Question 3 – Application of the equity method by a non-investment entity investor to an investment entity investee

The IASB proposes to amend IAS 28 to:

- (a) require a non-investment entity investor to retain, when applying the equity method, the fair value measurement applied by an investment entity associate to its interests in subsidiaries; and*
- (b) clarify that a non-investment entity investor that is a joint venturer in a joint venture that is an investment entity cannot, when applying the equity method, retain the fair value measurement applied by the investment entity joint venture to its interests in subsidiaries.*

Do you agree with the proposed amendments? Why or why not?

We disagree with the proposed amendments as we do not believe that an assumed difference in the practical difficulty of unwinding fair value measurements used by associates and joint ventures is a suitable basis for introducing a difference between applying the equity method to an associate and a joint venture when, as noted in paragraph BC22 of the Basis for Conclusions on the exposure draft, no such difference currently exists. It is true that, in some cases, underlying data may be more readily available for the investees of a joint venture investment entity than for an associate but this does not necessarily make that information more relevant or useful.

In addition, we note that the proposed amendment would be inconsistent with the requirement of paragraph 24 of IAS 28 not to remeasure a retained interest if an investment in an associate becomes an investment in a joint venture (or vice versa) as the proposed amendment would necessitate such a remeasurement.

As the equity method of accounting can validly be viewed as a valuation technique rather than as a one-line consolidation and on cost/benefit grounds, we recommend that fair value measurement be retained in applying the equity method to both associates and joint ventures that are investment entities.