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Investment entities

Consolidation accounting

8 January 2015

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Intermediate investment entities are the focus of these narrow-scope IFRS amendments

Highlights

- Consolidation of intermediate investment entities
- Consolidated financial statements exemption for intermediate parents owned by investment entities
- Policy choice for equity accounting for interests in investment entities
- Effective date – Annual periods beginning on or after 1 January 2016

New requirements for investment entities to use fair value accounting came into effect in early 2014, but early adoption had already highlighted a series of application issues.

In response, on 18 December 2014 the IASB issued Investment Entities: Applying the Consolidation Exception (Amendments to IFRS 10, IFRS 12 and IAS 28), which addresses three separate issues.

1. Intermediate investment entities

Should these entities be consolidated?

The extent of fair value accounting, rather than consolidation of subsidiaries, has been amended and is now as follows.

	Subsidiary does not provide investment-related services	Subsidiary provides investment-related services
Non-investment entity subsidiary	Fair value	Consolidated
Investment entity subsidiary	Fair value	**Fair value**

Before the amendment, it was unclear how to account for an investment entity subsidiary that provides investment-related services.

As a result of the amendment, intermediate investment entities are not permitted to be consolidated. So where an investment entity's internal structure uses intermediates, the financial statements will provide less granular information about investment performance – i.e. less granular fair values of, and cash flows from, the investments making up the underlying investment portfolio. As such, some simplicity has been achieved, but at the price of accounting that depends on internal structuring.

Many will see this as less useful and, as a result, some entities are likely to continue using parallel non-GAAP measures to meet the needs of their investors.

The IASB has also clarified that entities conducting 'investment-related services' are those whose main purpose and activities are to provide services that relate to the investment entity parent's activities.

2. Intermediate parents owned by investment entities

Consolidated financial statements exemption now available

Intermediate holding entities have a long-standing exemption from preparing consolidated financial statements when they are themselves consolidated by a higher parent (and when other relevant criteria are met).

In a welcome change, the amendments also make this exemption available to an intermediate held by an investment entity, even though the investment entity does not consolidate the intermediate.

3. Interests in investment entities

Policy choice available for equity accounting

A non-investment entity – e.g. a bank – may have a stake in an investment entity that it is required to equity account (typically as an associate). This gives rise to a question – should the bank's equity accounting pick up the investment entity's fair value accounting or pick up figures as if the investment entity had consolidated all of its subsidiaries?

The amendments settle this question by giving an accounting policy choice. This choice, which also comes as a welcome change, is based on practicability: it could be burdensome or even impractical to obtain a second set of financial statements on a consolidated basis solely for the purpose of equity accounting.

Effective date

The amendments apply retrospectively for annual periods beginning on or after 1 January 2016. Early adoption is permitted.