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**Re: Comment Letter on Investment Companies and Investment Entities**

Dear Ms. Seidman and Mr. Hoogervorst,

CFA Institute<sup>1</sup>, in consultation with its Corporate Disclosure Policy Council (“CDPC”)<sup>2</sup>, appreciates the opportunity to comment on the Financial Accounting Standards Board’s (“FASB”) Proposed Accounting Standards Update (“Proposed Update”), *Financial Services – Investment Companies (Topic 946): Amendments to the Scope, Measurement, and Disclosure Requirements* and the International Accounting Standards Board’s (“IASB”) Exposure Draft (“ED”), *Investment Entities*. The FASB Proposed Update and IASB ED are collectively referred to as the Proposals. The FASB and the IASB are collectively referred to as the Boards.

CFA Institute is comprised of more than 100,000 investment professional members, including portfolio managers, investment analysts, and advisors, worldwide. CFA Institute seeks to promote fair and transparent global capital markets and to advocate for investor protections. An integral part of our efforts toward meeting those goals is ensuring that the quality of corporate financial reporting and disclosures provided to investors and other end users is of high quality.

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<sup>1</sup> With offices in Charlottesville, New York, Hong Kong, and London, CFA Institute is a global, not-for-profit professional association of more than 107,000 investment analysts, portfolio managers, investment advisors, and other investment professionals in 137 countries, of whom nearly 96,000 hold the Chartered Financial Analyst® (CFA®) designation. The CFA Institute membership also includes 135 member societies in 58 countries and territories.

<sup>2</sup> The objective of the CDPC is to foster the integrity of financial markets through its efforts to address issues affecting the quality of financial reporting and disclosure worldwide. The CDPC is comprised of investment professionals with extensive expertise and experience in the global capital markets, some of whom are also CFA Institute member volunteers. In this capacity, the CDPC provides the practitioners’ perspective in the promotion of high-quality financial reporting and disclosures that meet the needs of investors.



### ***Joint Response to Proposals***

CFA Institute is issuing a joint comment letter on the IASB’s ED on Investment Entities and the FASB’s Proposed Update on Investment Companies due to the fact that one of the stated and primary objectives is to bring greater convergence to the treatment of such investment entities<sup>3</sup> under both International Financial Reporting Standards (“IFRS”) and U.S. Generally Accepted Accounting Standards (“U.S. GAAP”).

### ***Summary of Our Position***

CFA Institute commends the FASB and the IASB for taking a step in the right direction with respect to these Proposals. Below is a summary of the key positions which are described more fully in the remainder of the letter.

- 1) *Support Consolidation Exemption & Measurement of Investments at Fair Value* – CFA Institute agrees with the aspects of the Proposals which exempt investment entities from consolidating their investments and supports an approach where all investment entities report their investments at fair value through the profit and loss statement. Though we generally support consolidated financial statements, in the case of investment entities we favor specialized accounting where investments are carried at fair value (and not consolidated).
- 2) *Complexity & Lack of Convergence Raise Questions Regarding Whether Proposals Provide Most Decision-Useful Information For Investors* –
  - a) *Qualification Criteria Are Arbitrary “Accounting Rules”* – We are concerned that the six criteria established by the Boards to evaluate whether an entity qualifies for investment entity status will not capture all investment funds as these criteria are open to interpretive pressures, contain implicit options, provide for structuring opportunities and lack robustness. We also find that the Proposals draw accounting distinctions where economic distinctions do not necessarily exist.
  - b) *Multitude of Measurement & Presentation Differences Decrease Understanding & Comparability* – In our review of the Proposals we noted that because of the multitude of measurement and presentation methods and differences it is unlikely that investors and users of the investment entity financial statements will understand the results presented or be able to make comparisons among different investment entity financial statements. Specifically, we disagree with:
    - i. The IASB ED proposal to consolidate and, upon consolidation, change the measurement of investment entities when included in the financial statements of a non-investment entity parent.
    - ii. The U.S. GAAP Proposed Update requirement to consolidate investment entities in a fund-of-funds structure.
  - c) *U.S. GAAP & IFRS Differences Limit Comparability & Decision-Usefulness of Information* – From our evaluation and comparison of the Proposals,<sup>4</sup> our conclusion is that the complexity of the rules and the various measurement and presentation differences within and between U.S. GAAP and IFRS, along with challenge of understanding which entities qualify for these investment entity measurement and presentation methods, is so significant that users/investors may not be able to: a) evaluate the performance of the underlying investment portfolios; or b) compare the investment performance of different

<sup>3</sup> We use “investment entities” to refer to both investment entities and investment companies.

<sup>4</sup> We have illustrated these points diagrammatically in **Appendix I**.

investment entities. Investors must be able to evaluate and compare performance in order to make rational global investment allocation decisions. We believe the Proposals may have the unintended consequence of making evaluation of investment entities performance within and across entities and across jurisdictions difficult or impossible.

- d) *Disclosures Should Be Considered Only After Measurement & Presentation Issues Are Resolved, But Disclosures Should Be Consistent Between U.S. GAAP & IFRS* – We did not undertake a review of the proposed disclosure requirements or changes in the Proposals explicitly as we believe the measurement and presentation matters should be jointly addressed by the Boards before undertaking to evaluate the most meaningful disclosures. We do, however, believe the disclosures should be consistent between U.S. GAAP and we disagree with the IASB ED’s notion of simply articulating a disclosure principle.
- 3) *Re-evaluation Of Proposals By The Boards* – We urge the Boards in their re-deliberations to consider the issues raised in this comment letter, in particular the lack of convergence between IFRS and U.S. GAAP and the unnecessary complexity that has been introduced by the Proposals, which will result in inconsistent and non-comparable information for investment entities both within and across jurisdictions. Investment entity results need to be presented in a transparent, consistent and comparable manner for investors to ascertain and compare the underlying performance of the investments made by such entities.

#### ***Support Consolidation Exemption & Measurement of Investments at Fair Value***

CFA Institute agrees with the aspects of the Proposals which exempt investment entities from consolidating their investments and supports an approach where all investment entities report their investments at fair value through the profit and loss statement. Though we generally support consolidated financial statements, in the case of investment entities we favor specialized accounting where investments are carried at fair value (and not consolidated). We have previously articulated these views to the IASB and FASB<sup>5</sup> - views that have been mirrored by other constituents of the Boards. We commend the Boards for taking into consideration the concerns of their constituents and publishing these proposals for comment.

An investment entity’s primary business activity is buying, holding, and selling investments. And the objective of investors in investment entities is to earn returns (total returns) on their investments. Investors bear all the risk (positive and negative) of the investments and are interested in knowing the fair value of the investments and the change in fair value of those investments over time. Thus the results of the investment entity must be presented in a manner whereby investors can ascertain the underlying performance of the investments. The proposals for investment entities with measurement at fair value and the use of specialized accounting would therefore represent accounting that is consistent with the shareholder perspective.

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<sup>5</sup> We have expressed these views in the following documents:

- a) CFA Institute comment letter on ED 10, *Consolidated Financial Statements – Additional Comments Regarding Investment Companies*, October 22, 2009;
- b) CFA Institute comment letter in response to *Consultation on ESMA Technical Advice to the European Commission on Possible Implementing Measures of the Alternative Investment Fund Managers Directive*, September 13, 2011;
- c) CFA Institute letter to the FASB entitled *Follow-up to Meeting with Board 16 October: Consolidation Policy for Investment Companies and Investment Managers*, November 2, 2009.



The objective of financial reporting is to provide information that is relevant, comparable and decision-useful for investors in making their resource allocation decisions. For investment entities, we believe that reporting all of their assets and liabilities at fair value (with transparent reporting of fees and expenses) meets that objective. Rather than enhancing decision-useful information, consolidating the controlled investee may obscure decision-useful information and make it difficult for investors to evaluate performance. Non-consolidation with full disclosure of the underlying investments is, in our view, a superior approach.

Furthermore, the practicality argument often advanced against using fair value, either because of cost or the difficulty of estimating fair value for illiquid assets, does not apply in this case because investment companies use fair value accounting to report to their shareholders. Net asset value and the change in net asset value (often in comparison with a benchmark) is the primary metric that shareholders use to evaluate the performance of investment entities and to make buy and sell decisions.

We do have some concerns regarding the breadth of the definition regarding what constitutes an investment entity. Investment entities issue interests in the entity and use such proceeds to make investments in other companies. Other than incidental operating assets, all of their assets are invested and those investments should be reported at fair value. We urge the Boards to ensure that all entities with this business model qualify for investment entity status. As we note in **Appendix III** we have concerns that, under the current proposals, not all investment funds may qualify for investment entity status.

#### ***Greater Coordination & Convergence Required***

We commend the Boards for taking a step in the right direction with respect to these Proposals. However, while one of the objectives of the proposals is aligning IFRS and U.S. GAAP, there are several points of significant divergence that we believe will lead to differences in reporting by similar entities. When evaluating the Proposals in **Appendix I** we noted areas of divergence which are included in our complete consideration of the differences in the Proposals in **Appendix II**. We question whether the complexity of each of the Proposals, combined with their lack of convergence, achieves the maximum degree of possible decision-useful information for investors.

We urge the Boards to work more closely together as they re-deliberate the issues raised by the ED and Proposed Update. We also urge the Boards to issue their proposals at the same time. We believe the Boards should provide a more comprehensive and illustrative summary and comparison of the conclusions reached so that users and investors – as well as all other stakeholders – can quickly grasp the concepts deliberated, the conclusions reached, and any remaining differences.

As the Boards re-deliberate the issues associated with the IASB ED and the FASB Proposed Update, we ask that they step back from the detail and evaluate whether the accounting rules being contemplated truly reflect economic substance and provide adequate transparency to investors. We believe that the rules being proposed and the numerous differences between the IFRS and U.S. GAAP conclusions may not result in meeting these objectives.

***Analysis of Proposals – Will Investors Really Obtain The Most Decision-Useful Information?***

Our first step in undertaking a review of the IASB ED and the FASB Proposed Update was to attempt to visually depict the Proposals as shown in the diagrams in **Appendix I** so as to provide a complete picture of the accounting proposals under both IFRS and U.S. GAAP. We also made a comparison of the differences in the accounting for investment properties under IFRS (IAS 40, *Investment Property*) and the proposed guidance under U.S. GAAP (Proposed Update, *Investment Property Entities*) given their relationship to the Proposals.

Further, we evaluated the six criteria to be utilized to evaluate when an entity qualifies as an investment entity. Our evaluation of the qualifying criteria are included in **Appendix III**.

Below we make several observations with respect to the Proposals:

- 1) *Qualification Criteria Are Arbitrary “Accounting Rules”* – The Proposals establish six criteria to be utilized to evaluate when an entity qualifies as an investment entity. In **Appendix III** we articulate our various concerns with these criteria. In particular we note the following:
  - a) *Interpretive Issues, Implicit Options & Structuring Opportunities* – The proposed criteria to qualify as an investment entity are subjective in nature and will be subject to much interpretive pressure. Furthermore, the criteria contain implicit options, and therefore, may lead to structuring opportunities for entities depending on their desire to qualify as an investment entity.
  - b) *Lack Of Robust Criteria* – The qualification criteria within the Proposals contain criteria/language within them in order to achieve the Board’s desired outcome. The Proposals include language which is meant to include the entities the Boards’ wish to qualify as investment entities while scoping out other entities. The qualification criteria are such, however, that certain entities which have been traditionally considered investment entities may no longer qualify. We question the robustness of criteria that require these exceptions. Further, we do not believe these may result in cross-jurisdiction similarities when regulatory definitions of investment companies are scoped-in for U.S. GAAP but not for IFRS.

As we note in **Appendix I**, the Proposed Update on Investment Property Entities (IPEs) also contain qualification criteria with similar interpretive and optionality issues.

Overall, we question whether the qualification criteria – which will result in underlying differences in measurement and presentation – will present economically meaningful distinctions for investors or whether they will be manipulated to achieve management’s desired measurement and presentation objectives.

- 2) *Multitude of Measurement & Presentation Methods & Differences Decreases Understandability of Resulting Financial Statements to Investors* – Because of the multitude of measurement and presentation methods and differences it is unlikely that investors and users of the investment entity financial statements will understand the results presented or be able to make comparisons among different investment entity financial statements.

As noted previously, we evaluated the Proposals separately and jointly at **Appendix I**. Because the Proposals do not articulate or illustrate the accounting for:

- all the possible types of entities (e.g. investment companies, investment property entities, service providers, other investees, etc.);
- the levels of influence which may impact their accounting (e.g. control, significant influence, less than significant influence);
- the nature of the parent’s operations (e.g. investment company parent, non-investment company parent); and
- the importance of the investment entities structure/complex (e.g. fund-of-funds structure);

ascertaining the net result of the Proposals and the resulting differences is challenging for even the most technically skilled accountants. Further, the literature, and the language used (i.e. “specialized accounting”) does not make the discernment of these presentation vs. measurement differences from review of the literature easily discernible for investors.

Investors/users will not, we believe, be able to adjust for the measurement and presentation differences required by the accounting rules. As a result, investment entity financials may be less useful to investors than they should be.

Examples of the measurement and presentation differences, and our views on them, include:

- a) *Consolidation & Change In Underlying Measurement of Investment Entities By Non-Investment Entity Parent Under IFRS But Not U.S. GAAP* – The IASB ED proposes to consolidate and, upon consolidation, change the measurement of investment entities when included in the financial statements of a non-investment entity parent. We disagree with this proposal because: a) if fair value (without consolidation) was the most meaningful presentation for the subsidiary, the same measurement and presentation are equally meaningful at the parent entity’s level – irrespective of its other operations; b) consolidation is a presentation mechanism and not a measurement approach and investors will not understand this change in approach for this circumstance only.
- b) *Consolidation of Fund-of-Fund Investment Entities Under U.S. GAAP But Not IFRS* – For U.S. GAAP, the Proposed Update requires consolidation of investment entities in a fund-of-funds structure with retention of the specialized fair value accounting. For the reasons articulated above, we believe that fair value without consolidation and with supplementary information of underlying investments, if greater transparency is needed, is a preferable solution.
- c) *Net Asset Value as Practical Expedient for Fair Value Under U.S. GAAP But Not IFRS* – IFRS will require fair value while U.S. GAAP will allow use of net asset value (NAV) as a practical expedient. While we obviously prefer a fair value approach as an NAV approach differs from fair value due to liquidity adjustments, even if the underlying assets and liabilities are measured at fair value, we accept NAV as a practical expedient when the investment entity reports an NAV in which all or almost all of the underlying assets and liabilities are at fair value. In this circumstance, we believe the practical expedient is preferable to the determination of fair value by the investors, who may arrive at estimates of fair value that differ from estimates made by other investors in the same enterprise. For this reason, we believe the IASB should adopt this practical expedient rather than their being a difference between IFRS and U.S. GAAP. Where the NAV



includes significant underlying asset and liability measurements which are not at fair value, we do not believe the practical expedient is an appropriate alternative measurement to fair value. We believe that, in this case, the investee company should be required to provide an alternative NAV measurement in which all assets and liabilities are measured at fair value so that all investors report the same unit carrying value in the underlying investee. Consistency of IASB and FASB's conclusions and the alternate measurement are essential to comparability in a global investing environment.

- d) *Presentation & Measurement Differences for Service Providers & Other Investees* – There are measurement and presentation differences for service providers which are not helpful to investors. Service providers are consolidated on underlying IFRS or U.S. GAAP basis if control exists but if significant influence can be exercised they are at fair value for IFRS and equity method for U.S. GAAP. Further, the U.S. GAAP and IFRS investment entities guidance requires other investees to be measured at fair value but for investment property entities under U.S. GAAP these other investees (where there is neither control nor significant influence) are measured under other relevant U.S. GAAP. These differences cause unnecessary complexity and confusion and should be harmonized.

We also set forth in **Appendix I** measurement and presentation differences of concern related to Investment Property Entities.

- 3) *Complexity of Proposed Rules Combined With U.S. GAAP & IFRS Differences Limits Comparability & Decision-Usefulness of Information* – Our conclusion from our evaluation and comparison of the Proposals at **Appendix I** is that the complexity of the rules and the various measurement and presentation differences within and between U.S. GAAP and IFRS, along with challenge of understanding which entities qualify for these investment entity measurement and presentation methods, is so significant that users/investors may not be able to:
- evaluate the performance of the underlying investment portfolios;
  - compare the investment performance of different investment entities;

Investors must be able to evaluate and compare performance in order to make rational global investment allocation decisions.

Rather, we believe the Proposals may have the unintended consequence of making evaluation of investment entities performance within and across entities and across jurisdictions difficult or impossible.

- 4) *Differences Are Based Upon Arbitrary Accounting Rules Rather Than Economic Distinctions* – Our review of the Proposals finds that they draw accounting distinctions where economic distinctions do not necessarily exist as we describe more specifically in **Appendix I**. Broadly speaking, we find that these Proposals include accounting rules that create meaningless distinctions among investment entities, investment property entities, and operating entities, and the underlying measurement and presentation of their results which may result in artificial asymmetries, unnecessary complexities and reduced comparability across types of entities as noted in the proceeding section.

- 5) *Disclosures Should Be Considered Only After Measurement & Presentation Issues Are Resolved, But Disclosures Should Be Consistent Between U.S. GAAP & IFRS* – We did not undertake a review of the proposed disclosure requirements or changes in the Proposals explicitly as we believe the measurement and presentation matters should be jointly addressed by the Boards before undertaking to evaluate the most meaningful disclosures. We do not disagree with the additional disclosures proposed in the FASB Proposed Update, we just cannot fully comment on the necessary disclosures until issues such as whether fund-of-fund structures will be consolidated are jointly addressed. We do, however, disagree with the IASB ED’s notion of simply articulating a disclosure principle. We believe the IASB should undertake a comprehensive review of the U.S. GAAP disclosures related to investment companies and determine the disclosure requirements for investment entities more specifically. There absolutely must be consistency and symmetry of these disclosures.

***Proposals Should Be Evaluated By Boards Against Original Objectives:  
Are You Providing Investors With More Decision-Useful Information? &  
Did You Achieve Convergence?***

The Boards should jointly re-deliberate these Proposals and evaluate whether the proposed financial reporting reforms for investment entities have met the originally established objectives.

*Measurement & Presentation Differences & Complexities Limit Decision-Usefulness* – As we have already stated, the Boards have taken a positive first step with respect to the accounting for investment entities. However, given the unnecessary measurement and presentation differences and complexities that arrive from the Proposals, we urge the Boards in their re-deliberations to consider the objective of financial reporting in the context of investment entities.

Broadly, the objective of financial reporting is to provide information that is relevant, comparable and decision-useful for investors in making their resource allocation decisions. The conceptual basis which should guide the Boards’ decision-making in addressing investment entities is that the objective of investors in investment entities is to earn returns (total returns) on their investments. Investors bear all of the upside and downside risk of the investments and are interested in knowing the investments held by the company and the change in fair value of those investments over time. More simply, investors are interested in investment entity results being presented in a transparent manner whereby they can ascertain the underlying performance of the investments.

For investment entities, we believe that reporting all of their assets and liabilities at fair value (with transparent reporting of fees and expenses) meets that objective. As noted previously, our view has been that consolidating the controlled investee may obscure decision-useful information and make it difficult for investors to evaluate performance. Non-consolidation with full disclosure of the underlying investments is, in our view, a superior approach. This is what we believe the Boards should strive to achieve through their re-deliberations.





*Investing Is Global – Lack of Convergence in the Proposals Does Not Reflect This Reality* – It seems evident from the aforementioned items and the contents of **Appendix II** that the convergence objective has not been sufficiently achieved. The complexities of the Proposals and the resulting differences in U.S. GAAP and IFRS will make the accounting and reporting needlessly difficult for investors and users because the information provided will not be consistent or comparable across jurisdictions. In re-deliberating the Proposals, the Boards must evaluate each of the differences between U.S. GAAP and IFRS and evaluate whether there is sound economic justification for the differences and whether users and investors will benefit from such differences and the complexity and confusion they create. Our consideration of the differences suggests these are differences established by accounting standard setters not economic distinctions.

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Thank you again for the opportunity to comment on the IASB ED and FASB Proposed Update. If you or your staff have questions or seek further elaboration of our views, please contact either Mohini Singh, ACA, by phone at +1.434.951.4882, or by e-mail at [mohini.singh@cfainstitute.org](mailto:mohini.singh@cfainstitute.org) or Sandra J. Peters, CPA, CFA by phone at +1.212.754.8350 or by email at [sandra.peters@cfainstitute.org](mailto:sandra.peters@cfainstitute.org).

Sincerely,

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*/s/ Gerald I. White*  
Gerald I. White, CFA  
Chair  
Corporate Disclosure Policy Council

cc: Corporate Disclosure Policy Council

## *Evaluating the Complexity of the IASB & FASB Proposals*

### *Comparing & Evaluating the IASB & FASB Proposals*

*Visually Depicting the Proposals Illustrates Their Complexity* – Our first step in undertaking a review of the IASB ED and the FASB Proposed Update was to attempt to visually depict the proposals as shown in the diagrams on **Pages 16-19** so as to provide a complete picture of the accounting proposals under both IFRS and U.S. GAAP. We also made a comparison of the differences in the accounting for investment properties under IFRS (IAS 40, *Investment Properties*) and the proposed guidance under U.S. GAAP (Proposed Update, *Investment Property Entities*).

As neither the IASB ED nor the FASB Proposed Update clearly articulate – nor illustrate – the accounting for:

- all the possible types of entities (e.g. investment companies, investment property entities, service providers, other investees, etc.);
- the levels of influence which may impact their accounting (e.g. control, significant influence, less than significant influence);
- the nature of the parent’s operations (e.g. investment company parent, non-investment company parent); and
- the importance of the investment entities structure/complex (e.g. fund-of-funds structure);

the exercise illustrates and summarizes the complexity of the individual approaches.

### *Illustrations Demonstrate That Comparing IFRS and U.S. GAAP Proposals Is Challenging* –

Even more challenging than depicting the IASB ED and FASB Proposed Update separately, is preparing or illustrating the proposals in a manner which facilitates a comparison such that a complete articulation of the differences between IFRS and U.S. GAAP can be discerned. The complexity is only compounded when the net result of IASB ED and FASB Proposed Update are compared. Our conclusion is that even the most technically inclined accountants may be challenged to make such comparisons.

Investors/users will not, we believe, be able to adjust for the measurement and presentation differences required by the accounting rules. As a result, investment entity financials may be less useful to investors than they should be.

### *Measurement vs. Presentation Issues Will Be Difficult for Investors/Users To Discern*

Also challenging to investors will be the nomenclature and terminology which does not make readily apparent the importance of distinction between:

- i) Measurement – The underlying measurement basis which is being addressed or discussed (e.g. fair value, NAV, percentage of ownership of underlying equity value, cost, etc.); and
- ii) Presentation – The presentation method being proposed (e.g. consolidation with gross presentation, equity method, fair value, “specialized accounting,” etc.).

When evaluating the proposals, it is challenging, at times, to determine if the accounting issue is one of measurement or presentation or measurement and presentation because the same

terminology may be utilized in two different contexts. For example, “specialized accounting” can be used by some to mean that investment companies are allowed to use fair value and by others to mean that investment companies use fair value and they don’t consolidate. Fair value is traditionally used to refer to how an investee will be measured, but it also articulates the form of presentation without explicitly being thought of as an expression of presentation. The term “specialized accounting” is made more confusing by the notion under the Proposed Update that an investment company would consolidate another investment company in a fund-of-funds structure and present the investments and related minority interests gross, but at their fair value (i.e. thereby retaining “specialized accounting” when the term is used only to refer to fair value).

Making this issue even more confusing is the IASB ED’s notion that you consolidate an investment entity and change its underlying measurement basis when it is owned by a non-investment entity parent. This “violates” what accountants traditionally view as the theory of consolidation which is simply changing the presentation from net (i.e. equity method) to gross (i.e. consolidation) presentation. Consolidation, heretofore, has not been thought of as process of changing measurement. If this is not commonplace to accountants, it will certainly not be a concept readily apparent to investors.

*Differences Are Based Upon Accounting Rules Rather Than Economic Distinctions* – As we review the proposals, we find that they draw accounting distinctions where economic distinctions do not exist. Examples include:

- 1) Allowing definitional criteria – which can be “managed” or contain “implicit optionality” – to determine whether an entity is within the scope of an investment entity and whether it applies fair value (i.e. the most relevant measure) or consolidates its underlying investees illustrates this point most vividly as the nature of the entity that owns the underlying asset does not change its economic value despite the accounting rule requiring different measurement.
- 2) Consolidating and changing the measurement of an investment entity by a non-investment entity parent is a further illustration of the aforementioned point. Again, the nature of the parent’s operations does not change the value of the underlying investment.
- 3) Treating fund-of-funds structures differently under U.S. GAAP (consolidate) and IFRS (do not consolidate) is another example. Economically, if you own a percentage interest then you should reflect the percentage interest and, if more disclosure is required of the underlying investment, then provide it. Additionally, the difference between U.S GAAP and IFRS does not seem to be based upon an economic distinction.
- 4) Only reflecting investment properties at fair value on an optional basis for IFRS, but requiring they be at fair value for U.S. GAAP if “housed” within an investment property entity is an arbitrary accounting rule. There is no difference in the value of the investment property because of the choice of the option or the nature of the entity owning it.
- 5) Maintaining different definitions of investment properties under U.S. GAAP (total return) and IFRS (investment income and total return) is an example of an accounting versus and economic distinction. The accounting standards governing the preparation of the financial statements should not arbitrarily define the measurement used, they should require the economic measurement.



Broadly speaking, we find that these Proposals include accounting rules that create false distinctions among investment entities, investment property entities, and operating entities, and the underlying measurement and presentation of their result may result in artificial asymmetries, unnecessary complexities and reduced comparability across types of entities.

*Complexities & Lack of Convergence Will Limit Decision-Useful Information For Investors & Users* – The purpose of the IASB ED’s on investment entities and the FASB Proposed Update’s on investment companies and investment property entities was to address the complaints of a number of constituents regarding the decision-usefulness of investment entity financial statements. These constituents, including CFA Institute, believed that rather than enhancing decision-useful information, consolidating the controlled investee actually obscures such information and makes it impossible for investors to evaluate performance. The other objective of these projects was to broadly align IFRS and U.S. GAAP accounting and presentation for such investment entities and investment properties. Simultaneously, the Boards sought to be mindful of the accounting being developed for lessors under the Leases Project.

Set forth in the following sections we describe some of our observations on the detailed complexities of both the investment company and investment property proposals under both U.S. GAAP and IFRS as well as the challenges presented by the lack of their convergence that will also increase complexity.

We urge the Boards in their re-deliberations of the Proposals to address these complexities and the lack of convergence as we believe they limit the decision-usefulness of the information being provided to investors.

#### ***Investment Entities – Specific Considerations***

**Pages 18 and 20** visually depict the differences in the FASB and IASB Proposals on the accounting for investment companies and investment entities, respectively. Summarized below are the major differences, complications, and complexities associated with the differences in accounting for investment entities guidance.

*Disagree With Consolidation & Change In Underlying Measurement of Investment Entities By Non-Investment Entity Parent Under IFRS But Not U.S. GAAP* – The IASB ED extends the consolidation exception to the parent of an investment entity provided that the parent qualifies as an investment entity itself. It does not allow the consolidation exception to be carried through to a parent that is not itself an investment entity. The non-investment entity parent is required to apply normal consolidation guidance to all the entities it controls, including those that are controlled by the investment entity subsidiary. Still further, the IASB ED requires the non-investment entity parent to not only consolidate the underlying entity (e.g. gross-up the presentation), it requires that the underlying measurement basis of the investment entity being consolidated be changed from fair value, other than if a service provider, to the existing IFRS guidance in-place for the measurement of underlying assets and liabilities outside of investment entities. Substantively, this has the effect of distorting the most relevant view (net presentation of the investment) and measurement (fair value) of the underlying assets.

We believe that the non-investment entity parent should be able to retain the specialized accounting applied by its subsidiary investment entity, consistent with the FASB Proposed Update. If fair value provides the most relevant and decision-useful information in the financial statements of the investment entity, then it will also provide the most decision-useful information in the group's financial statements.

Moreover, from an operational perspective, obtaining the information required for consolidation of a controlled investment entity is likely to be far more burdensome than obtaining fair value information and require the maintenance of two sets of financial information, which is cost prohibitive and will be borne by the investors.<sup>6</sup> While we have frequently argued that investors are willing to pay for the preparation of decision-useful financial statements, we do not believe they are willing to pay for information that hinders such decisions.

The IASB ED's Basis for Conclusion states that consolidation by the non-investment is an anti-abuse measure because a parent could selectively make investments through an investment entity to avoid consolidation and alter the measurement basis. The IASB ED notes that disallowing the consolidation exemption to a non-investment entity parent addresses this issue. However, we suggest that preserving the specialized accounting of the investment entity subsidiary with full disclosure of the underlying investments is a superior approach to addressing any structuring opportunities while providing investors with decision-useful information. Disclosure of the underlying investments will shed light on any material abuses of this exception.

*Disagree With Presentation & Measurement Differences for Service Providers & Other Investees –*

- *Non Fair Value Accounting for Investees Providing Services & Difference in Accounting for Service Providers Where There is Significant Influence* – Both the IASB and FASB proposals have specific requirements with respect to investees providing services that relate only to the investment entity's own investment activities. If the investment entity has a controlled subsidiary that provides such services, then the subsidiary will be consolidated while all other subsidiaries will still be measured at fair value. Unlike the FASB proposal, which requires a service provider over which the investment entity has significant influence to be accounted for under the equity method, the IASB proposal requires fair value accounting, thereby creating another accounting difference. We urge the Boards to require the use of a single measurement basis for all investees – fair value, as it is the most relevant measurement basis – and to ensure there is convergence on all aspects of the measurement of entities.

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<sup>6</sup> Though the IASB ED proposes to restrict extending the consolidation exception to non-investment entity parents, the IASB believes it would nonetheless be available in most cases because the IASB believes that in most cases investment entities do not have non-investment entity parents. We contend, however, that it is unlikely for a conglomerate and its subsidiaries to meet the definition of an investment entity and that there are clearly circumstances where these entities hold controlling interests in investment entities. For example, some investment entities may have a parent that is a bank or an insurance company or another non-investment entity where the presentation and measurement of the underlying investment entity at fair value is most relevant. We also envisage situations in which an investment manager will control the investment fund under IFRS 10, *Consolidated Financial Statements*, and will therefore be required to consolidate all the subsidiaries of the investment fund that are accounted by the fund at fair value.

- *Other Investees* – The FASB Proposed Update on Investment Companies requires all other investees over which the parent investment company has neither control nor significant influence to be measured at fair value. On the other hand, the FASB Proposed Update on IPEs requires all other investees over which the parent IPE has neither control nor significant influence to be measured in accordance with other relevant U.S. GAAP. Again, we urge the Boards to require the use of a single measurement basis for all investees – fair value.

*Fair Value under IFRS vs. Net Asset Value under U.S. GAAP Will Result in Unnecessary Measurement Differences* – Another difference between the IFRS and U.S. GAAP approaches is that U.S. GAAP allows the use of net asset value as a practical expedient for fair value in the case where the underlying investee “strikes” an NAV. IFRS will not allow such an expedient. As a result, there will be a difference between NAV and fair value for identical investments. Generally, this is a simple liquidity adjustment if all the underlying assets and liabilities are at fair value. When the underlying assets and liabilities are not at fair value under U.S. GAAP, there will also be a difference between U.S. GAAP and IFRS associated with the measurement differences between NAV and fair value.

When the investment entity reports an NAV in which all or almost all of the underlying assets and liabilities are at fair value, we believe the practical expedient is preferable to the determination of fair value by the investors, who may arrive at estimates of fair value that differ from estimates made by other investors in the same enterprise. For this reason, we believe the IASB should adopt this practical expedient.

Where the NAV includes significant underlying asset and liability measurements which are not at fair value, we do not believe the practical expedient is an appropriate alternative measurement to fair value. We believe that, in this case, the investee company should be required to provide an alternative NAV measurement in which all assets and liabilities are measured at fair value so that all investors report the same unit carrying value in the underlying investee.

Consistency of IASB and FASB’s conclusions and the alternate measurement are essential to comparability in a global investing environment.

*Disagree With Consolidation of Fund-of-Fund Investments Entities Under U.S. GAAP & Divergence from IFRS* – Under the FASB Proposed Update, an investment company that has a controlling financial interest in another investment company or an investment entity in a fund-of-funds structure has to consolidate its controlling interest retaining the underlying specialized accounting measurement but reflecting the investments at fair value on a gross basis with a minority interest.<sup>7</sup> While we understand that the purpose of the FASB’s requirement to consolidate investment companies in a fund-of-funds structure is to increase the transparency as to the nature of the underlying investments, we believe the consolidation, and resulting gross presentation, won’t substantially improve the transparency to investors. Rather, it may serve to

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<sup>7</sup> The FASB has not defined a “fund-of-funds” structure in its Master Glossary or the Proposed Update. It is therefore unclear how an investment company will ascertain whether its controlling financial interest in another investment company or an IPE is in a fund-of-funds structure or not.





decrease transparency by not allowing investors insight into the appropriate proportion of their investment. As result, we do not favor the FASB's Proposed Update in this regard.

An investment company does not invest in another investment company in order to control it, but rather to seek an efficient mechanism to gain exposure to expertise within a specific sector or asset class or as a mechanism to efficiently develop an asset allocation strategy.<sup>8</sup> We suggest that preserving the specialized accounting of the investment entity subsidiary with full disclosure of the underlying investments is a superior approach to consolidating all the investment entities in a fund-of-funds structure.

Further, the resulting difference between U.S. GAAP and IFRS on this point will only serve to further decrease comparability for investors and for that reason convergence should be sought on this issue. This difference is not based upon economic differences and should be converged.

### ***Investment Properties – Specific Considerations***

**Pages 19 and 21** visually depict the differences in the IASB and FASB guidance on the accounting for investment property entities. Summarized below are the major differences, complications, and complexities associated with the differences in accounting for investment properties guidance.

#### ***IASB (Asset-Based & Optional Use of Fair Value) vs.***

***FASB (Entity-Based & Required Use of Fair Value) Guidance*** – The IASB “asset-based” guidance applies to investment properties irrespective of the entity owning the properties, but includes an option to measure investment properties at either fair value or cost. The FASB proposed guidance is an “entity-based” approach that requires entities meeting the definition of an “investment property entity” to measure their investment properties at fair value. Our view has been that the nature of the entity or management’s intent does not change the value of an investment property nor what it should be valued at in the financial statements. Accordingly, such distinction only creates unnecessary complexity and reduces comparability for investors and other users of the financial statements.

***IASB vs. FASB Definition of Investment Properties*** – In addition to the existence of differences associated with the FASB vs. IASB models being “entity vs. asset-based” approaches and the FASB guidance requiring the use of fair value while the IASB guidance allows fair value to be an optional election, the IASB and FASB have different definitions of what constitutes investment properties. The FASB focuses solely on total return while the IASB allows investment property to be held for receipt of income as well as total return. Our view is that maintaining different definitions of investment property under U.S. GAAP and IFRS is not consistent with economic reality. We do not believe that investment property is purchased without considering the ultimate value as well as the periodic income. Thus, the IASB view would result in accounting, rather than economic, distinctions which produce less decision-useful and comparable information to investors.

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<sup>8</sup> Please see AICPA Investment Companies Task Force comment letter to the FASB on the FASB’s website.



*Criteria to Be an Investment Property Entity Subject to Interpretative Issues, Create Implicit Optionality & Create Accounting Rather Than Economic Distinctions* – As we more fully explain in our comment letter on the FASB’s Proposed Update on Investment Property Entities, the proposed guidance includes various requirements used to define an investment property entity which are subject to significant interpretative issues, create implicit optionality and establish accounting rather than economic distinctions. The complexities created by these “rules,” and the lack of convergence, does not benefit investors in the investment decision-making process.

*FASB Provides Further Entity Specific Accounting for IPE Investees Which Differs from U.S. GAAP Accounting for These Entities* – The FASB’s proposed guidance includes rules regarding how to account for an investment property entity’s ownership interests in investees. Some of these “rules” are just that, rules, which are not consistent with investment company guidance (e.g. the use of relevant U.S. GAAP rather than fair value for all investees/financial interests where there is no control or significant influence and the consolidation of investment companies and investment property entities irrespective of the fund-of-funds structure where there is control) in certain circumstances and consistent with investment company guidance in other circumstances (e.g. the use of fair value for other investees where there is control or significant influence and the use of equity or consolidation for service providers where there is significant influence or control).

The overall result is a mixture of investment company accounting and traditional U.S. GAAP which, when layered on to the complexity of the definition of an IPE, will only make the decision-usefulness and comparability of this information more challenging for investors and other users.

*FASB Approach Improperly Focuses Stakeholders on Real Estate Owned by Investment Companies Rather Than the Appropriate Measurement (Fair Value) of Investment Properties* – The FASB’s entity-based approach also improperly focuses stakeholders attention on the need to measure investment properties at fair value only for those entities who are akin to investment companies (e.g. those that strike a net asset value). This is evident through stakeholders comments that the proposed investment properties guidance should be included within, subsumed into or made a part of the investment companies guidance. This thinking misses the broader issue. That issue being: What is the most relevant measure of investment properties – irrespective of the form of entity which owns them? The most relevant measure is fair value and the form of entity and management intent are not determinates in that measurement.

*Recent Examples of Relevance of Fair Value Information Across a Spectrum of Entities Demonstrates Need for Fair Value Information Related to Real Estate* – In our comment letter on the FASB’s Proposed Update on Investment Property Entities, we provide several recent and poignant examples of where real estate fair values have been unequivocally relevant to the valuation of the enterprise – irrespective of management intent or the nature of the enterprise. The examples provide empirical evidence regarding the relevance of fair value information in the investment decision-making process across a broad spectrum of enterprises.

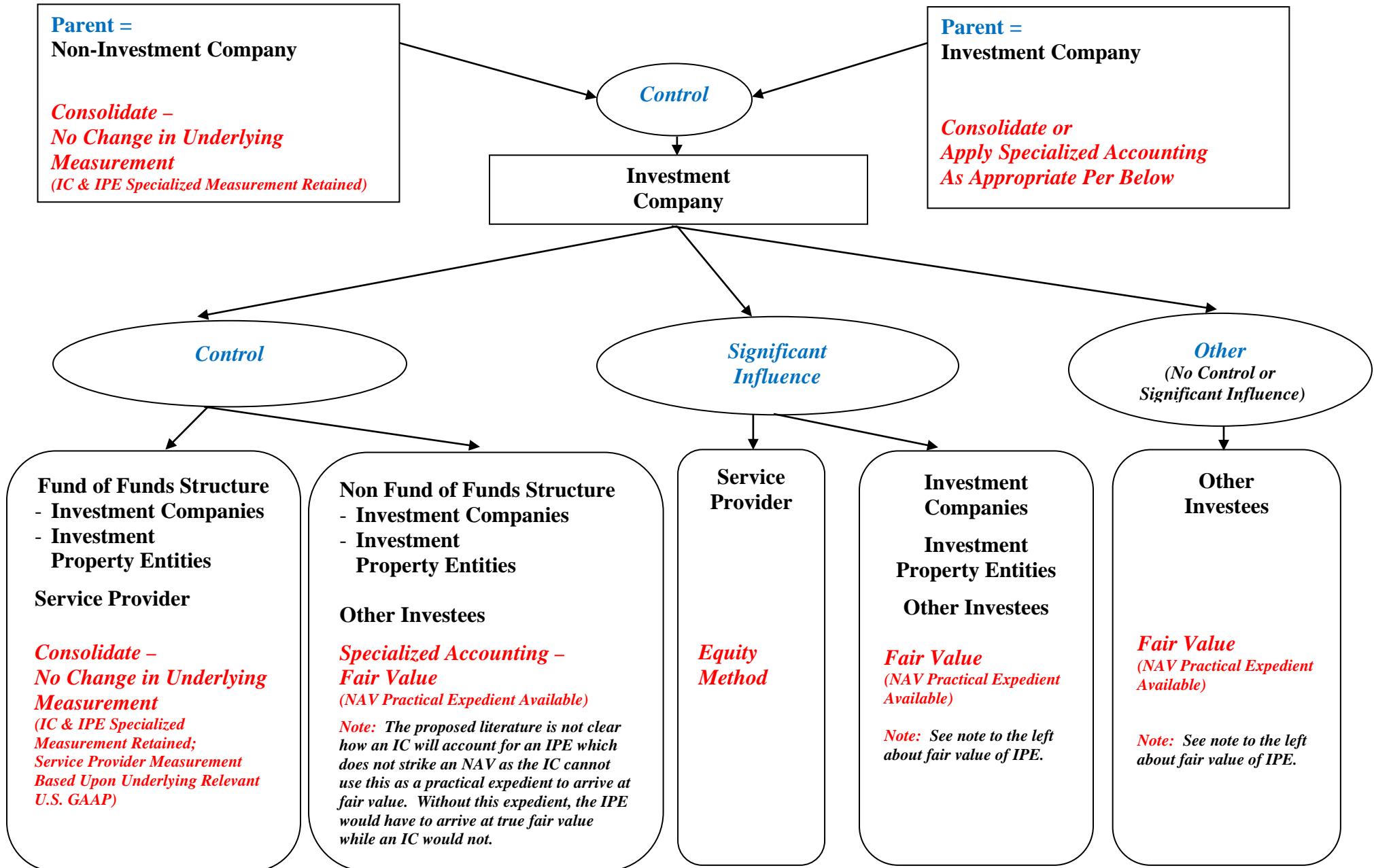


*IASB & FASB Should Converge on an Asset-Based Approach Which Requires Fair Value For Investment Properties and Disclosure of Fair Value for All Real Estate* – For the aforementioned reasons, we believe the complexities of the FASB’s proposal on investment property entities combined with the lack of convergence will only limit the decision-usefulness of information provided. Few investors are going to undertake the exercise to discern all of the aforementioned accounting distinctions. The complexities created by the IASB and FASB approaches along with their lack of convergence are not beneficial to investors as they creating accounting rather than economic distinctions and reduce comparability.

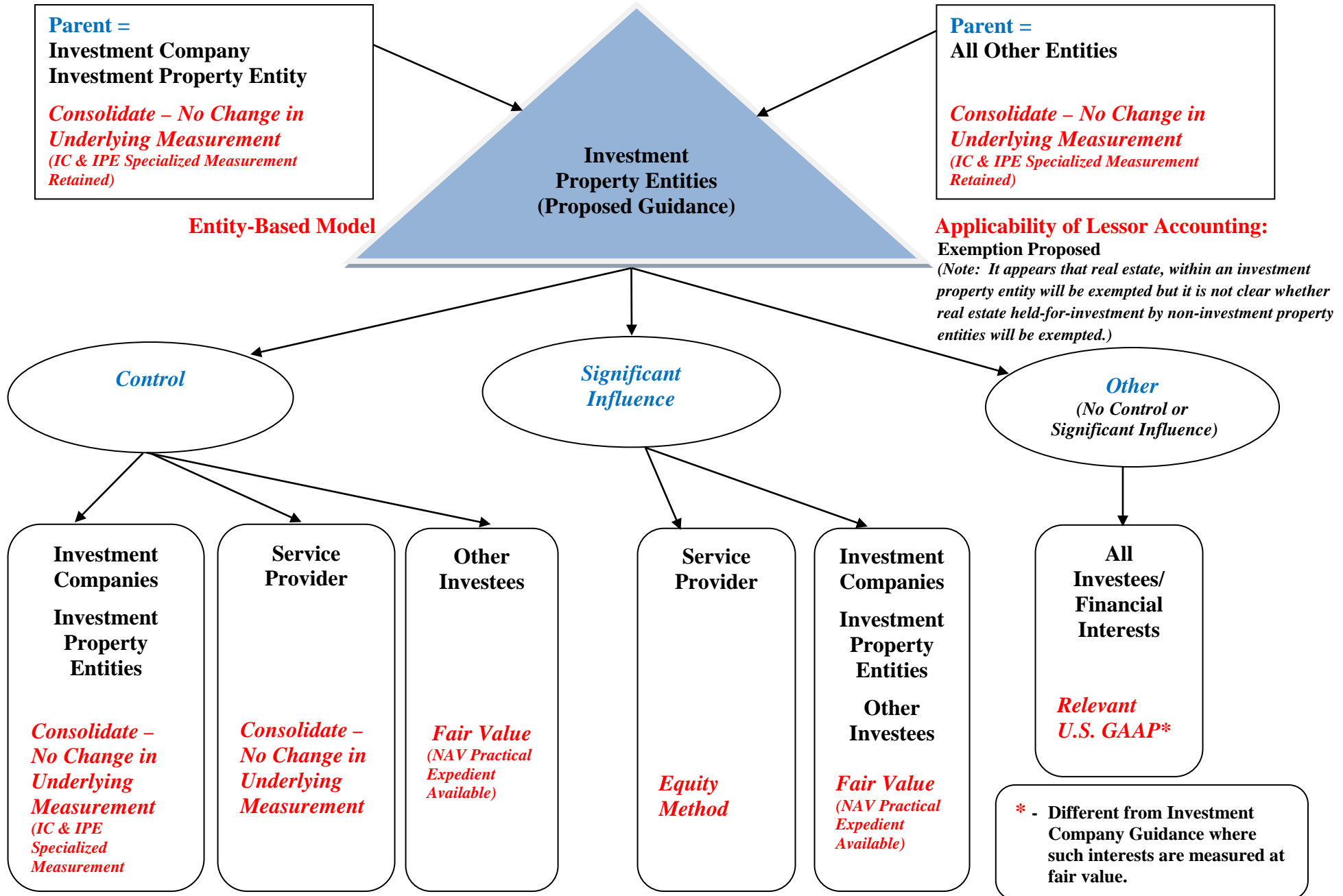
It is our view that an asset-based approach focused on the fair value for all real estate is the optimal solution. Reasonable intermediate steps which require, rather than allow the optional application of, fair value for investment properties using an asset-based approach with a broader definition of investment properties (i.e. income and total return) is more appropriate than the entity-based approach in the Proposed Update. The FASB needs to go further, however, and at a minimum require the parenthetical disclosure on the face of the financial statements of audited fair values of real estate properties. An annual disclosure with update upon significant interim economic events would be an improvement over the current state of reporting and disclosure.

*Comment Letter on Investment Property Entities* – Our complete comments on the FASB’s Proposed Update on Investment Property Entities can be found in our comment letter to the FASB which may be accessed at the FASB or CFA Institute’s websites.

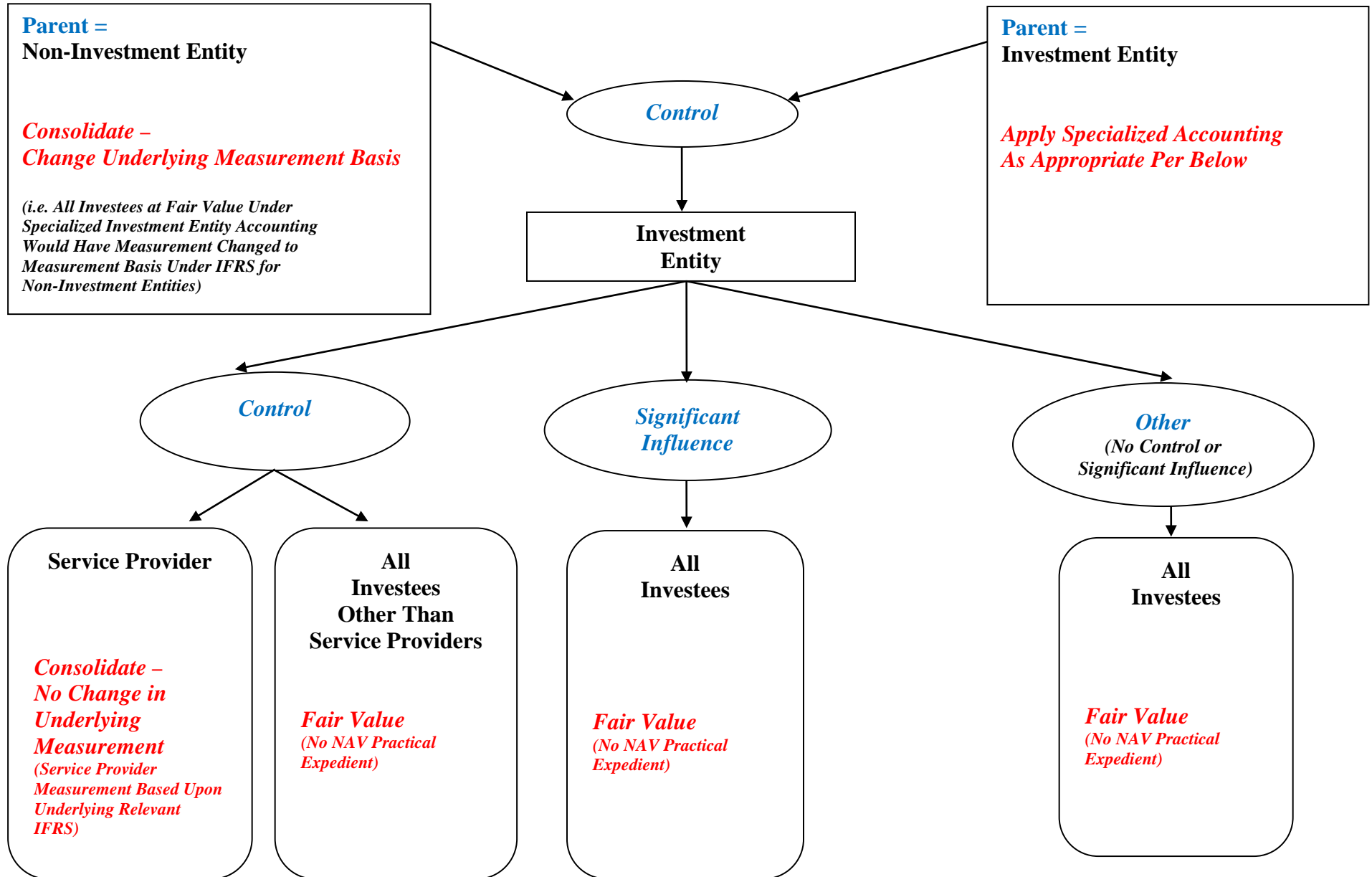
**U.S. Generally Accepted Accounting Principles (U.S. GAAP) – Investment Companies**



**U.S. Generally Accepted Accounting Principles (U.S. GAAP) – Investment Properties**

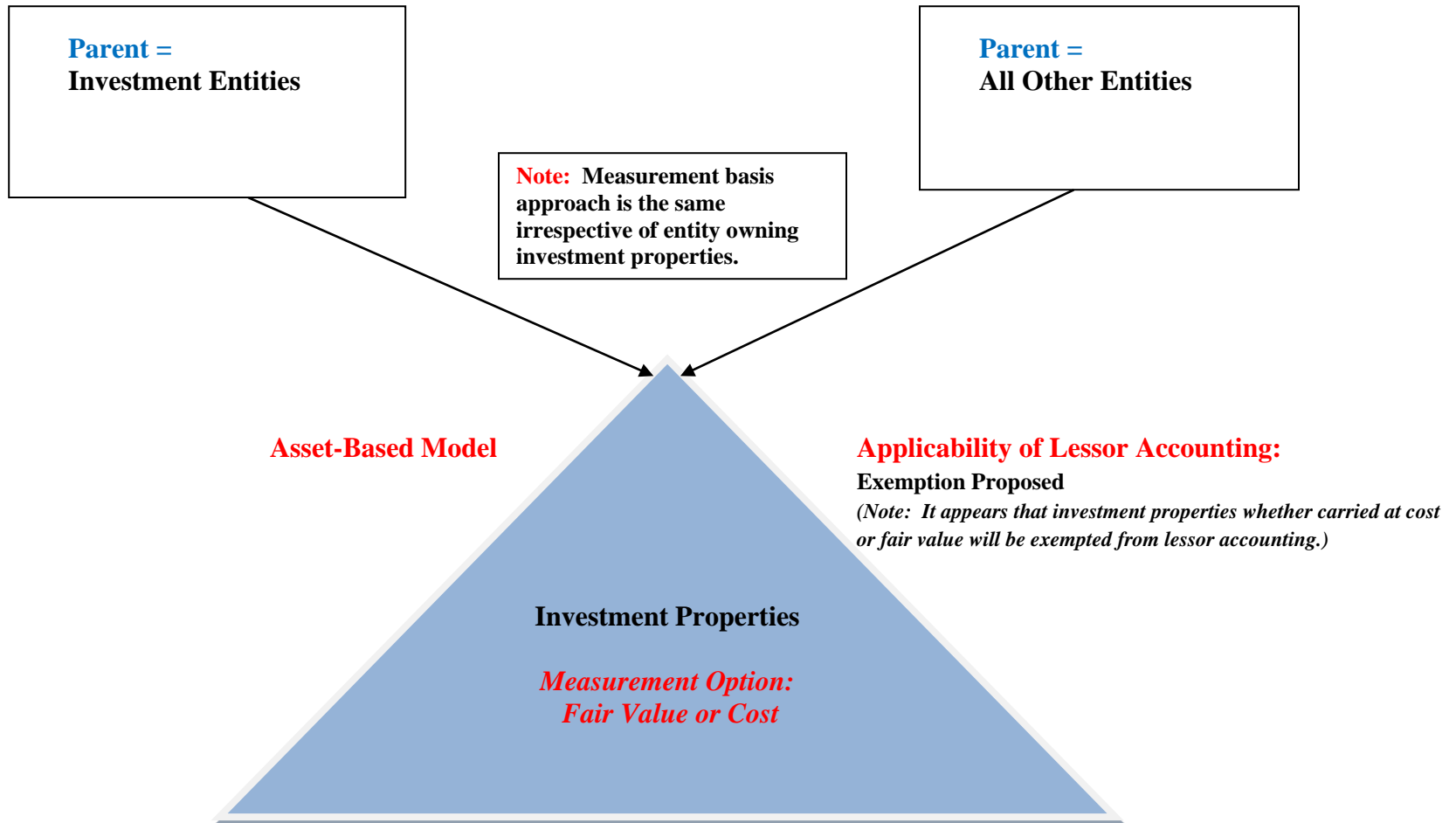


*International Financial Reporting Standards (IFRS) – Investment Entities*





*International Financial Reporting Standards (IFRS) – Investment Properties*



### *Understanding The Degree of Convergence*

While one of the stated objectives of the IASB ED and FASB Proposed Update is aligning IFRS and U.S. GAAP, we note several significant points of divergence that we believe will lead to differences in reporting by similar entities. We urge the Boards to address the differences listed below:

#### *Consolidation By Non-Investment Entity Parent Company*

- Under the IASB ED, the consolidation exception does not extend to the parent of an investment entity that is not itself an investment entity and the basis of accounting of the investment entity subsidiary is changed.
- The FASB Proposed Update requires the parent of an investment company that is not itself an investment company to consolidate the investment company subsidiary but allows retention of the specialized accounting of the subsidiary.
- Under the IASB ED and FASB Proposed Update, the specialized accounting will be retained when a non-investment entity parent is accounting for its interest in an investment entity over which it has significant influence.

In our view, the IASB ED should be amended to converge with that of the FASB's Proposed Update. We believe that the non-investment entity parent should be able to retain the specialized accounting applied by its subsidiary investment entity, consistent with the FASB Proposed Update. Because fair value provides the most decision-useful information in the financial statements of the investment entity, it will also provide the most decision-useful information in the group's financial statements.

#### *Controlled Investees in Fund-of-Funds Structure Will Be Consolidated*

- The FASB Proposed Update requires an investment company to account for its controlling interests in other investment companies and IPEs in a fund-of-funds structure in accordance with Topic 810, *Consolidation*. Investment company and IPE subsidiaries not in a fund-of-funds structure are not consolidated.
- The IASB ED does not make the distinction of an investment company subsidiary of a parent investment company within or outside of a fund-of-funds structure. Under the IASB ED the investment company subsidiary is not consolidated and the specialized accounting is retained.

As a result of this difference, there will be greater consolidation under the FASB Proposed Update than under the IASB ED.

### Service Providers

- The FASB Proposed Update makes a distinction for an entity that provides advisory services to its parent that is an investment company. When the parent investment company has control the service provider is consolidated and when the parent investment company can exercise significant influence the equity method is applied.
- The IASB ED only makes this distinction in the case of a controlled service provider. No such distinction is made where the parent investment entity can exercise significant influence. In this case, the service provider is measured at fair value.

As a result of this difference, there will be inconsistency of the treatment of service providers under U.S. GAAP and IFRS where there is significant influence. Also, the most relevant measure – fair value – will not be used for IFRS or U.S. GAAP.

### Net Asset Value Expedient

- U.S. GAAP requires an investment company to measure its underlying investments at fair value and provides a practical expedient that permits an entity with an interest in an investment entity to use NAV as fair value in specific circumstances.
- The IASB ED does not permit this practical expedient.

As a result, there will be a difference between NAV and fair value for identical investments. Generally, this is simply a liquidity adjustment if all the underlying assets and liabilities are at fair value. When the underlying assets and liabilities are not at fair value under U.S. GAAP, there will also be a difference between U.S. GAAP and IFRS associated with the measurement differences between NAV and fair value.

### Application to Regulated Funds

- The IASB ED only applies to entities that meet the definition of an investment entity. There is no accommodation for regulated funds to qualify for investment entity status without meeting all of the criteria.
- Per the FASB Proposed Update, an investment company that is regulated under the Investment Company Act of 1940 would be subject to the investment company guidance regardless of whether the entity meets the proposed definition of an investment company.

We question the robustness of the qualification criteria that do not capture all regulated investment companies and the difference in treatment where the IASB does not scope-in all regulated investment companies.

### Application of Investment Property Guidance

- If an investment company meets the criteria to be an investment property entity in the FASB's Proposed Update on Investment Property Entities, it will apply the requirements in that proposed update.
- The IASB has not proposed specific guidance to define an IPE. Therefore, the entity would apply the proposed investment entity requirements under IFRS that would require the entity to account for its investment properties in accordance with IAS 40, *Investment Property*.

Consequently, the reporting by such an entity would be different under U.S. GAAP and IFRS. The consequences of those differences are more fully illustrated and discussed in **Appendix I**.

### Measurement of Investment Transactions

- The IASB ED requires investment transactions to be recorded at fair value both upon initial recognition and subsequently.
- Per the FASB Proposed Update, investment transactions will initially be recorded at transaction price with subsequent measurement at fair value.

We do not believe there is a conceptual justification for recording the same transaction with different measurement approaches for initial measurement and subsequent measurement. We believe there should be a single measurement approach and we believe that fair value is the appropriate measurement basis. Therefore, the FASB proposal should be amended to converge with the IASB position.

### Cost of Disposed Securities

- The IASB ED does not prescribe how to calculate the cost of disposed securities.
- The FASB Proposed Update requires an investment company to determine the cost of disposed securities using the average cost of the securities or by specifically identifying the cost of each security sold.

The amount of realized gain (or loss) on the disposal of a security could be different under U.S. GAAP and IFRS depending on the method used to determine the cost of the security that was disposed.

### Disclosures

- Much of the U.S. GAAP guidance on investment company disclosures, such as what information to include in an investment company's financial highlights and directions on how to calculate the highlights, is not included in the IASB ED as a requirement.
- The IASB ED includes a disclosure principle to enable investors to evaluate the nature and results of an entity's investment activities. The proposal does provide recommendations that mirror U.S. GAAP requirements. For example, it recommends disclosures similar to a statement of investments and financial highlights

Thus an investment entity applying IFRS might ultimately disclose less or different information than it would under U.S. GAAP.

We do not believe the disclosure principle in the IASB ED will lead to sufficient disclosures. Specific disclosure requirements should be included to accompany the principle.



### *Financial Statement Presentation*

#### *Overall Presentation Requirements*

- Specific financial statement presentation requirements will exist for an investment company applying U.S. GAAP, including guidance on realized and unrealized gains and losses and the provision for income taxes.
- The IFRS proposal does not include the same financial statement presentation requirements.

This will likely result in different financial statement captions between U.S. GAAP and IFRS and will affect the comparability of financial information.

#### *Rental Revenue and Related Expenses*

- The FASB Proposed Update includes a requirement that investment companies recognize rental revenue arising from the lease of a real estate property in accordance with the contractual terms of the related lease separate from related expenses.
- The IASB ED does not require this presentation on a gross basis.

### *Consideration of the Qualification Criteria*

The Proposals establish six criteria for determining when an entity qualifies as an investment entity. The Proposals require that the only substantive activity of an investment entity be to invest for capital appreciation and/or investment income. The Boards' intention is for the guidance to apply only in a narrowly defined set of circumstances.

*Not All Investment Funds May Qualify As Investment Entities*<sup>9</sup> – We believe that because of the narrow criteria and restrictions placed on business activities not all investment funds will actually qualify as investment entities. Examples of activities that preclude investment entity status are included in both the Proposed Update and the IASB ED. Below are several matters for consideration:

- 1) *Private Equity Funds May or Many Not Be Included* – Some private equity funds may indeed benefit from the proposal by becoming investment entities. However, we wonder whether the IASB and FASB have considered the possible range of private equity activities – from appointment of directors of the controlled investee to more active involvement in assisting to restructure the operations of the investee – that may disqualify them from attaining investment entity status.
- 2) *Collateralized Debt and Loan Obligations May No Longer Qualify* – Currently, under the FASB Codification, a collateralized loan obligation (CLO) would be considered an investment company based on a pooling of funds from numerous investors, even though most of those investments are in the form of debt. However, the requirement in the Proposed Update is that investors obtain ownership interests. This requirement may, therefore, represent a significant change in practice for collateralized debt obligations (CDOs) and CLOs that currently employ investment company reporting. While those CDOs and CLOs could avail themselves of the fair value option to account for their investments, they would nonetheless not qualify for the specialized financial statement presentation of an investment entity. The FASB's Proposed Update and the IASB ED are consistent in their approach to these CDOs and CLOs.
- 3) *May Be Difficult for Certain Real Estate Funds To Qualify Because of Their Activities* – Under the IASB ED, it may be difficult for real estate funds to qualify as investment entities because of the range of activities often undertaken with respect to the operations of controlled investees. Real estate funds are often involved in activities such as construction and redevelopment. Entities involved in these activities are precluded from attaining investment entity status.

Under the FASB Proposed Update if an entity were allowed to perform activities that support its investing activities, then a real estate fund or real estate investment trust (that is not an investment property entity) could be an investment company provided the entity (directly or indirectly through an agent) manages only properties that it owns (i.e. it is allowed to perform activities that support its investing activities). However, if the other activities did more than support the entity's investment activities – for example, construction or warehousing activities – this would preclude the entity from being an investment company.

Additionally, the fair value management criterion requires that substantially all of the investment company's investments are managed, and their performance evaluated, on a fair value basis. Many geared real estate funds manage the underlying assets of the investee on a fair value basis but manage any debt in the structure at amortized cost. It is unclear whether, in certain circumstances, these geared funds would qualify as investment entities as the debt is not managed on a fair value basis.

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<sup>9</sup> KPMG, *New on the Horizon: Investment Entities*, September 2011.



*Criteria Will Be Subject To Interpretive Pressure* – We believe that the qualification criteria will come under significant interpretive pressure. For example, consider a situation in which one of the criteria (e.g. managing investments on a fair value basis) is not met for one investment that represents ten percent of the portfolio but is not managed on a fair value basis. It appears this would preclude investment entity status. However, would an insignificant violation be acceptable? If so, at what level does it become unacceptable?<sup>10</sup>

*Implicit Options* – The proposed investment entity qualifying criteria contain implicit options which may lead to structuring opportunities for entities – allowing the entities to opt in or out of the guidance’s scope. Utilizing the express business purpose criterion as an example, entities may believe they can present themselves to investors as an investment entity within the guidance simply based upon their “expression” of their business purpose. If entities attempt to view the wording of this criterion as providing an option to qualify as an investment entity based upon their “expression of business purpose,” it will create an implicit option with respect to their application of this guidance.

*Exceptions to the Qualification Criteria Raise Question Regarding Their Robustness* – Exceptions have been incorporated within the qualification criteria in order to attain the desired outcomes. We question the robustness of criteria that require exceptions such as those noted below:

- 1) *Pooling of Funds Criteria Not Required To Be Met If Owned By Investment Entity* – One criterion for determining whether an entity is an investment entity is that there be a pooling of funds. However, the Proposals permit an entity whose single investor is an investment entity to still be considered an investment entity provided that:
  - a. Under that IASB guidance, it meets all of the other qualification criteria.
  - b. Under the FASB guidance, the entity is formed in conjunction with an investment entity parent that itself has third party investors that, in aggregate, hold a significant unrelated interest in the parent.This exception to the pooling of funds criterion is required to help address certain investment fund structures, such as, a master-feeder structure where the master fund is formed with a single investor that is an investment entity (i.e. a feeder fund that has several unrelated investors).
- 2) *Investment Company’s Under ’40 Act Are Investment Company’s Irrespective of Whether The Fit the Criteria* – Per the FASB Proposed Update, an investment company that is regulated under the Investment Company Act of 1940 would be subject to the Investment Company guidance regardless of whether the entity meets the proposed definition of an investment company. In particular, we question the vigor of qualification criteria that do not capture all regulated investment companies.<sup>11</sup>

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<sup>10</sup> KPMG, *New on the Horizon: Investment Entities*, September 2011.

<sup>11</sup> The IASB proposal provides no similar requirement that all regulated funds qualify for investment entity status without meeting all of the criteria.