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Mr Hans Hoogervorst, Chairman
International Accounting Standards Board (IASB)
30 Cannon Street
London EC4M 6XH
United Kingdom

16 January 2015

Dear Mr Hoogervorst,

On behalf of the Austrian Financial Reporting and Auditing Committee (AFRAC), the privately organised standard-setting body for financial reporting and auditing standards in Austria, we appreciate the opportunity to comment on the Exposure Draft ED/2014/4 *Measuring Quoted Investments in Subsidiaries, Joint Ventures and Associates at Fair Value*.

Principal authors of this comment letter were Max Eibensteiner, Christian Höllerschmid and Erich Kandler. The professional background of these authors is heterogeneous (two preparers and one auditor) in order to assure a balanced Austrian view on the ED.

GENERAL REMARKS

We support the Board's efforts to clarify the measurement of quoted equity investments in order to avoid unnecessary diversity in practice. Even though this ED is primarily concerned with entities applying the consolidation exemption for investment entities under IFRS 10, the issue of measuring quoted equity investments at fair value is not limited to the accounting for investments in subsidiaries, joint ventures and associates in separate financial statements in accordance with IAS 27. It may also be relevant in other situations, such as step acquisitions, or disposals of subsidiaries while retaining an equity-accounted interest, spin-offs or distributions to owners of quoted equity investments in accordance with IFRIC 17 etc. Consequently, the Board's assumption that the impact of the ED would be limited should be reconsidered.

We fully support the ED's definition of the unit of account as the investment as a whole (i.e., a package of financial instruments) rather than the individual financial instruments making up that investment. Only a package of financial instruments – if of sufficient size – gives the investor control. However we do not share the Board's conclusion that, despite this unit-of-account definition, the fair value of such a package of financial instruments shall be measured at fair value as the product of the quantity of instruments held (Q) and the quoted price for the individual instrument without any adjustments (P). This approach is conceptually flawed as it contradicts the Board's definition of the unit of account and does not reflect the underlying economics of the nature of an equity investor's relationship with its investee properly (i.e., the difference between holding a purely financial investment and holding a strategic investment).

As far as Level 1 fair value measurements of groups of financial assets and financial liabilities whose market risks are substantially the same are concerned, however, we support the ED's proposal, because the key characteristics of such portfolios and the measurement issues involved are of different kinds to the ones arising from packages of financial instruments making up investments in subsidiaries, joint ventures or associates.

SPECIFIC REMARKS

Question 1—The unit of account for investments in subsidiaries, joint ventures and associates

The IASB concluded that the unit of account for investments within the scope of IFRS 10, IAS 27 and IAS 28 is the investment as a whole rather than the individual financial instruments included within that investment (see paragraphs BC3–BC7).

Do you agree with the proposed amendment? Why or why not? If not, what alternative do you propose?

We agree with the ED's conclusion and the proposed amendment. In BC6, the IASB states that the nature of an equity investor's relationship with an investee is the key characteristic feature of investments in subsidiaries, joint ventures and associates. In other words, only a package of financial instruments can give an investor significant influence, and possibly control. The level of

control or influence over the investee conferred by a package of shares is thus a compelling argument in favour of the unit of account being the investment as a whole.

We believe that this clarification with regards to the unit of account is compelling enough to be included in the standard's body, and not only in the basis for conclusions. Moreover, we believe that measurement requirements consistent with the unit of account must be capable of capturing this key characteristic feature.

Question 2—Interaction between Level 1 inputs and the unit of account for investments in subsidiaries, joint ventures and associates

The IASB proposes to amend IFRS 10, IFRS 12, IAS 27 and IAS 28 to clarify that the fair value measurement of quoted investments in subsidiaries, joint ventures and associates should be the product of the quoted price (P) multiplied by the quantity of financial instruments held (Q), or P × Q, without adjustments (see paragraphs BC8–BC14).

Do you agree with the proposed amendments? If not, why and what alternative do you propose? Please explain your reasons, including commenting on the usefulness of the information provided to users of financial statements.

Since we agree with the ED's definition of the appropriate unit of account, we disagree with the Board's conclusion that irrespective of the definition of the unit of account the fair value of the package of (quoted) financial instruments should be calculated by simply multiplying the quantity (Q) of the instruments held the quoted price (P) without any further adjustments. We think that this is incompatible with the unit of account being the investment as a whole. This conclusion also ignores the fact that there is no Level 1 measure for this defined unit of account.

We recognise that the quoted price for an individual financial instrument and the quantity held by an investor may be observed and verified easily. The proposed approach would therefore allow auditors and users of financial statements to verify this measure and makes fair value measurement less arbitrary. Nevertheless, this measure does not reflect the equity investor's relationship with its investee and introduces volatility into the accounting for investments in subsidiaries, joint ventures and associates. We believe that introducing such volatility does not provide relevant nor reliable information and impairs fair presentation. We still agree, however, that an observable quoted price for the individual financial instrument should be the starting point for the fair value measurement of a package of financial instruments.

The ED states that the nature of an equity investor's relationship with its investee is the key characteristic feature for investments in subsidiaries, joint ventures and associates. The level of control or influence in the investee conferred by a package of shares is thus a compelling reason for the unit of account being the investment as a whole. This key characteristic feature – assuming the package is sufficiently large – can only be reflected in a fair value measure deviating from Level 1 measurement, as there is no fair value that can be established for the package of financial instruments that is considered the relevant unit of account.

The level of influence is generally reflected in the excess of any exit price for a package of financial instruments over the sum of the quoted prices of all individual financial instruments included in the package multiplied by the quantity held. The amount of this excess is commonly referred to as a control premium. IFRS 13 mentions such premia as possible reasons for adjustments of non-Level 1 fair values where the premia reflect key characteristics of the assets being measured and would, therefore, be taken into account by market participants acting in their economic best interest. In the case of an equity investment of sufficiently large size (where the sum of its components would constitute the appropriate unit of account), the level of influence conveyed by the control premium would typically be taken into consideration by market participants.

Provided that there is sufficient empirical evidence from capital markets to assess the amount of an industry-specific control premium, control premia should be taken into account when measuring the fair value of a package of quoted equity investments. In our view, a Level 2 measurement would thus be appropriate. At the same time, we believe that the empirical evidence used for assessing the control premium should be closely linked to the specific size of the package, the ownership structure of the entity's equity instruments being measured and the relevant industry.

Taking into consideration the relevance of control premia for market participants, we believe that the ED's proposal would lead to a situation where different facts and circumstances (related to level of control or influence over the investee) would be dealt with in a uniform way, thus failing to reflect their diversity. Making different things look alike neither improves faithful presentation nor increases the relevance of financial information provided.

In addition to the specific issue dealt with in the ED, we would suggest also clarifying the somewhat ambiguous treatment of premia and discounts in IFRS 13, because in some places it is said that premia and discounts may be reflected in fair value measures, whereas in other parts this is prohibited (see IFRS 13.69 and 13.80). We believe that this ambiguity could be removed by incorporating the proposed unit-of-account definition into the body of the standard. It is also set out in IFRS 13 that size by itself does not constitute an appropriate basis for adjustments, but the control premium, a key characteristic of investments in subsidiaries, joint ventures and associates, is definitely related to the size of a share package of financial instruments – depending, of course, on how widely ownership of the remaining shares is distributed.

All in all, we think that the issue under consideration, particularly the accounting for risk premia, needs some revision in order to make the Board's intentions clearer and to make consistent application of IFRS 13 easier. In the light of the issues raised above, we suggest adding some specific guidance on possible ways of adjusting Level 1 fair values for individual financial instruments for premia and discounts in order to find an appropriate measurement for the relevant unit of account. To maintain objectivity, such guidance could, e.g., be restricted to market-based adjustments. Control premia could then, e.g., be measured on the basis of transactions in comparable packages of financial instruments in the relevant industry, thus avoiding Level 3 control premia that are derived solely from modelling.

Question 3—Measuring the fair value of a CGU that corresponds to a quoted entity

The IASB proposes to align the fair value measurement of a quoted CGU to the fair value measurement of a quoted investment. It proposes to amend IAS 36 to clarify that the recoverable amount of a CGU that corresponds to a quoted entity measured on the basis of fair value less costs of disposal should be the product of the quoted price (P) multiplied by the quantity of financial instruments held (Q), or P × Q, without adjustments (see paragraphs BC15–BC19). To determine fair value less costs of disposal, disposal costs are deducted from the fair value amount measured on this basis.

Do you agree with the proposed amendments? If not, why and what alternative do you propose?

For similar reasons to those set out above, we do not agree with the ED's proposal. When determining the selling price of a quoted CGU, the reporting entity should be allowed to include a premium (or a discount) on the quoted CGU's value. Such adjustments should, however, be justified by the size of the package of financial instruments making up the quoted CGU. Furthermore, sufficient empirical evidence from capital markets should be required to confirm that the premia or discounts could be realised in the event of a sale as at the valuation date.

Question 4—Portfolios

The IASB proposes to include an illustrative example to IFRS 13 to illustrate the application of paragraph 48 of that Standard to a group of financial assets and financial liabilities whose market risks are substantially the same and whose fair value measurement is categorised within Level 1 of the fair value hierarchy. The example illustrates that the fair value of an entity's net exposure to market risks arising from such a group of financial assets and financial liabilities is to be measured in accordance with the corresponding Level 1 prices.

Do you think that the proposed additional illustrative example for IFRS 13 illustrates the application of paragraph 48 of IFRS 13? If not, why and what alternative do you propose?

We support the inclusion of the illustrative example clarifying the application of IFRS 13.48 in the context in question. However, this amendment addresses an issue different from the one related to the fair value measurement of quoted investments in subsidiaries, joint ventures and associates and should thus be dealt with separately (e.g., as part of annual improvements): where such portfolios are measured without reference to investments in subsidiaries, joint ventures and associates, the measurement issue that mainly arises is linked to illustrating an entity's net exposure to market risk and not to reflecting an equity investor's relationship to its investee.

Question 5—Transition provisions

The IASB proposes that for the amendments to IFRS 10, IAS 27 and IAS 28, an entity should adjust its opening retained earnings, or other component of equity, as appropriate, to

account for any difference between the previous carrying amount of the quoted investment(s) in subsidiaries, joint ventures or associates and the carrying amount of those quoted investment(s) at the beginning of the reporting period in which the amendments are applied. The IASB proposes that the amendments to IFRS 12 and IAS 36 should be applied prospectively.

The IASB also proposes disclosure requirements on transition (see paragraphs BC32–BC33) and to permit early application (see paragraph BC35).

Do you agree with the transition methods proposed (see paragraphs BC30–BC35)? If not, why and what alternative do you propose?

As the clarifications proposed by the ED refer to IFRS 13, and the transitional provisions for this standard were to be applied prospectively, we suggest applying the same provisions for all amendments to standards that are imposed by the current ED. The transitional provisions must also be considered in the light of the fact that this ED potentially affects fair value measurements when applying IFRS 3, IFRS 5 or IFRIC 17.

Kind regards,

Romuald Bertl,

Chairman