COMMENTS

24 September 2008

CONCEPTUAL FRAMEWORK: THE REPORTING ENTITY

General remarks

BUSINESSEUROPE believes that the Discussion Paper provides valuable insight into the issues it raises. We support that the Framework includes a broad description of the reporting entity and agree with the broad description proposed; (subject to the choice between view 1/view 2 in response to the reporting entity concept).

We also believe that as a preliminary step to defining the boundaries of a reporting entity, the Board should explain how consolidated financial statements best fulfil the objective of financial reporting; this – probably basic and non controversial – introduction would serve as a reference to determine the appropriate model to retain at the conceptual level, and help solve issues at the standard's level.

BUSINESSEUROPE supports that the Framework gives guidance to identify the composition of a group; we believe however that more discussion and analysis are needed before it can be concluded that the control model should be retained; we disagree that the risks and rewards model is set aside without a proper analysis.

We are in broad agreement with the definition of control proposed; we believe however that the implications of shared control should be considered at the conceptual level; while absolute power is acknowledged as rather theoretical, conceptual thinking is missing in assessing what limitations prevent the power criterion to verify while other limitations let it be met.

BUSINESSEUROPE believes that an in-depth analysis and debate are needed before deciding on the perspective (parent-company perspective or entity perspective) from which financial statements should be prepared, and, lastly, we do believe that neither consolidated accounts nor separate parent company accounts are self-sufficient in fulfilling the needs of users; decisions to be made in this area should take this inter-dependency into account.

Detailed comments

Section 1: The reporting entity concept (questions 1 & 2)

BUSINESSEUROPE supports the IASB's efforts in including a definition/description of a reporting entity in the conceptual framework, as the notion is central to financial reporting. We agree that the description should not refer to the legal form of the entity,

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for the reasons explained in the DP, notably the approach to economic substance has precedence over legal form.

In addition, we wonder whether this definition would lead to undesirable and unidentified consequences. As a result, we would rather recommend that it is not introduced in the framework.

Section 2: Group reporting entity

Selecting the model (questions 3 & 5)

Before addressing how to define a group reporting entity, BUSINESSEUROPE believes that a discussion of how and why aggregating reporting entities as if they were one brings useful information to capital providers. We gather that such discussion would be rather basic and non controversial. However such a discussion should serve as reference in selecting the appropriate model and refining the model selected, either at the conceptual level or at the standard's level.

BUSINESSEUROPE understands that the IASB has set its preference for the control model long ago and does not intend to devote a lot of staff and Board time to the discussion. We do not believe that the discussion in the paper truly provides a sound and comprehensive basis to assess whether the control model should be retained. We observe that the risks and rewards model is not really discussed and that the main reason for leaving it aside is that it would require substantial work to make it a robust basis. Although this may be a valid reason not to retain it for the time being, we disagree that this would serve as a justification to make a well informed choice at the conceptual level. If this is the only effort that the IASB can provide for the time being, the issue should remain for the record not yet assessed. We disagree however that the risks and rewards model (beyond acting as a supplement to the control model) be dropped as a possible model without a proper analysis.

Under the assumption that the control model is retained (questions 4, 6 & 7)
As requested by the invitation for comment, all our comments below are made on the assumption that the control model is retained.

BUSINESSEUROPE agrees that control should be defined at the conceptual level and that the definition of control should refer to both power and benefits. Economic phenomena are of interest to users insofar they can have an impact on the performance and financial position of the entity. We believe however that the power criterion should be analysed in greater depth. Although the DP specifically mentions that power does not need to be absolute, guidance is needed to assess (at the standard's level or in practice) how the power criterion verifies. Such a discussion would also be helpful to address in a more principle-based manner the issue of joint control (par 159 – 161).

Moreover, we find the discussion of the control concept at both the asset and entity levels rather confusing and as a result rather unconvincing. In particular we disagree with paragraph 57, as it seems to us that a difference should be made between the definition/description of an entity (i.e. a circumscribed area of business activity, in the current IASB thinking) and the definition of the boundaries of an entity. That difference prevents the reference to control from being circular. Our understanding of the justification of the control model is that having control of an entity would provide control of the assets and the liabilities of that entity. The draft exposure draft of the future consolidation standard states in paragraph 11 "*The consolidated financial statements present the assets and liabilities controlled by the parent,…* ". We think this issue requires clarification.

In the context of the control model, we agree that the controlling entity model should be used as the primary basis for determining the composition of a group entity. We believe that the common control model should constitute an extension of the controlling entity model, in situations where that model would not be appropriate and when combined financial statements would bring useful financial reporting to capital providers.

Section 3: Parent entity financial reporting

Should the entity perspective govern the presentation of financial statements? (Question 8)

BUSINESSEUROPE is concerned that the Board continues to push forward and implement at standard's level (IFRS 3 R and IAS 27 R) the entity's perspective without addressing the debate appropriately. The only argument which is put forward in favour of the entity's perspective is that it serves the needs of all capital providers, not only the investors in the parent company. We are not convinced by that argument. We believe that only capital providers to the parent company (either shareholders or lenders or others) find consolidated financial statements useful. Other capital providers to the group will find more relevant information to their needs in the financial statements of subsidiaries in which they have placed their interests. We therefore believe that all capital providers that find consolidated financial statements useful find the parent's company perspective relevant.

Furthermore we are all the more concerned by the decision of the Board that the staff has considered not appropriate to deal with this issue at present, because they are not in a position, *at this stage,* to thoroughly assess all the consequences of the change.
We therefore recommend to leave the issue pending until the necessary analysis and debate can take place.

Parent-only financial statements (Questions 9 & 10)

Although BUSINESSEUROPE agrees that consolidated financial statements are useful (question 9), we do not consider them as able to fulfil all the needs of capital providers. Parent-only financial statements are useful too for the reasons explained in the DP (par 128 -129). We therefore would oppose a conceptual framework that would preclude their presentation.

BUSINESSEUROPE believes that defining the form in which the two sets of reporting should be presented does not belong to the conceptual framework, but should be addressed at the standard's level. The conceptual framework should state that a set of financial statements that does not include all information relevant to the needs of capital providers is not complete and should not be provided without clear reference to the necessary supplementary information.

Section 4: Control issues (questions 11 & 12)

The assessment of control is in our view similar to any other assessment of an economic situation, all facts and circumstances need to be taken into account (a). As a result the concept of control needs to be a broad concept (c). This is in our view what makes principle-based standards different from rule-based requirements. That is what helps meet the substance over form principle.
We would agree that temporary control is control; however we believe a principle-based reference is needed to define whether consolidated financial statements are useful in all situations where the entity has control. This would help to properly assess the consequence of control being temporary before concluding that consolidated financial statements are useful (b). It would also help define whether consolidated financial statements of entities held in a capital risk context are useful. The principle-based reference would best sit in the framework, while the consequences to draw from it would be addressed valuably at the standard's level (question 12).
We fully concur with the analysis in par 155 -156 (d) and believe that the distinction between holding an option and holding the underlying rights after exercise is a very useful and far-reaching issue that is best addressed at the conceptual level (question 12).

BUSINESSEUROPE believes that more work in the present conceptual phase is needed before valuable conclusions can be reached on e) and f). Furthermore the Board should analyse why and how consolidated financial statements would not present useful information to capital providers when, from an economic point of view, there is no difference in how subsidiaries and joint ventures are combined to optimise the group's future cash flows, and where the limitations brought by a situation of shared power are not necessarily more restrictive than the rights granted to minority interests by the legal framework of a jurisdiction. Such an analysis would provide useful insight to either the strengths of the control model or its weaknesses. In our view, no conclusion should be drawn on ED9 before the necessary conceptual analysis has been carried out.

Please refer to our recommendations set in our answers to questions 3 (1st paragraph) and 4 (2nd paragraph).