

Date  
3 October 2008

Le Président

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des Experts  
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Dear Mr. Enevoldsen,

**Re: EFRAG Draft Comment Letter on Discussion Paper *Preliminary Views on an improved Conceptual Framework for Financial Reporting: The Reporting Entity***

1. FEE (Fédération des Experts Comptables Européens - Federation of European Accountants) is pleased to submit its comments on the EFRAG Draft Comment Letter on the Discussion Paper *Preliminary Views on an improved Conceptual Framework for Financial Reporting: The Reporting Entity* (the "DP").
2. We welcome the Board developing the concept of a reporting entity for inclusion in the new Conceptual Framework. It is logical for the Framework to contain a description or definition of a reporting entity. Like EFRAG, we agree with the DP's proposal that the Framework should contain a broad description of a reporting entity. We are also content with the broad description proposed.
3. We share EFRAG's concern that control as defined in the DP should be used as the basis for determining the composition of a group reporting entity. In our opinion, the controlling entity model should be considered in conjunction with the risks and rewards approach to determine the composition of a group reporting entity. Like EFRAG, we recommend that the IASB carry out further work on the notions of control and risks and rewards in order to develop a single concept which includes both notions. We also agree that this notion be dealt with at the Framework level.
4. The Exposure Draft "An improved Conceptual Framework for Financial Reporting - Chapter 1 and Chapter 2" expresses the view that financial reporting should reflect the entity perspective rather than the perspective of the owners of the entity. We strongly support EFRAG's view that a full debate is needed on the perspective from which financial statements should be prepared, before a conclusion can be reached at this stage of the Framework project. In particular, we are like EFRAG not supportive of the proprietary approach. However, although we see more merits in the entity approach since this is a principles-based model, we believe that the practical consequences of such a model need further thought in particular on issues like the dividing line between equity and debt and the treatment of goodwill under IFRS 3. Also the practicalities of such a model need further consideration.

5. We agree that there should be a basic definition of control defined at the conceptual level and that it should refer to both power and benefits. Another key aspect of the definition that should be clarified at the conceptual level is whether consolidation arises when an entity controls at the present time another entity or whether it arises when the investor has at the present time the ability to obtain control over another entity. There seems that some confusion is derived by the fact that the DP defines control has “having the *ability* to determine...” while indicating in paragraph 154 of the DP that “the ability to take control” does not translate in having control at the present time. The proposed definition needs to be sufficiently coherent with the standards, for example with IAS 27 on Consolidation. We think that the link to the Consolidation project is important as an example of how the IASB should ensure that any proposed definition works in practice. Until there is sufficient evidence of this, we suggest the IASB consider deferring issuance of the revised Standard on Consolidation. We believe that EFRAG should make this link to the Consolidation project explicit in its Comment Letter.
6. Finally, we agree that there is a need to allow the preparation of general purpose “group” financial statements in certain circumstances not captured by the controlling entity model.
7. Our responses to the questions in the Invitation to comment Section of the DP are contained in the Appendix to this letter.

We would be pleased to discuss any aspect of this letter that you may wish to raise with us.

Yours sincerely,



Jacques Potdevin  
President

Ref: ACC/JP/SS/LF

**Appendix: Responses to the questions in the Invitation to comment - Discussion Paper  
Preliminary Views on an improved Conceptual Framework for Financial  
Reporting: The Reporting Entity**

**Question 1**

**Do you agree that what constitutes a reporting entity should not be limited to business activities that are structured as legal entities? If not, why?**

8. We agree with EFRAG that what constitutes a reporting entity should not be limited to business activities that are structured as legal entities.

**Question 2**

**Do you agree that the conceptual framework should broadly describe (rather than precisely define) a reporting entity as a circumscribed area of business activity of interest to present and potential equity investors, lenders and other capital providers? If not, why? For example, do you believe that the conceptual framework should establish a precise definition of a reporting entity? If so, how would you define the term? Do you disagree with including reference to equity investors, lenders and other capital providers in the description (or definition) of a reporting entity? If so, why?**

*Should the Framework contain some sort of description or definition of a reporting entity?*

9. It is logical for the Framework to contain a description or definition of a reporting entity.
10. In addition, we agree with EFRAG and the DP that it is for each jurisdiction to decide which entities should be required to provide regular financial reports and what form these reports should take.

*Is the broad description of a reporting entity proposed in the DP sufficient and appropriate?*

11. We think that EFRAG's developments in paragraphs 6 and 7 of its Draft Comment Letter could be read as causing some confusion about the reasons why EFRAG seems at the end to consider a broad description of a reporting entity as a circumscribed area of business activity, rather than a precise definition, is a satisfactory way to capture the subject of a reporting entity.
12. We support the broad description of a reporting entity proposed in the DP as sufficient and appropriate at this stage.

*The reference to capital providers in the description (or definition) of a reporting entity*

13. We agree with the inclusion of a reference to equity investors, lenders and other capital providers in the description of a reporting entity.
14. Even if we agree with the concept used in the definition of a reporting entity, we wonder whether the words chosen (in particular "business activities") could be interpreted as not encompassing not-for-profit and non-commercial entities.

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**Question 3**

**Do you agree that the risks and rewards model does not provide a conceptually robust basis for determining the composition of a group reporting entity and that, except to the extent that it overlaps with the controlling entity model (as discussed in paragraphs 102 and 103), the risks and rewards model should not be considered further in the reporting entity phase of the conceptual framework project? If not, why?**

15. We agree with EFRAG that control on its own is not sufficient in all circumstances. In our opinion, the controlling entity model should be considered in conjunction with the risks and rewards approach to determine the composition of a group reporting entity. As EFRAG points out, this may prove useful in circumstances when it is difficult to determine whether control exists. Like EFRAG we recommend the IASB to carry out further work on the notions of control and risks and rewards in order to develop a single concept which includes both notions. We also agree that this notion be dealt with at the Framework level.
16. Another key aspect of the definition that should be clarified at the conceptual level is whether consolidation arises when an entity controls at the present time another entity or whether it arises when the investor has at the present time the ability to obtain control over another entity. There seems that some confusion is derived by the fact that the DP defines control as "having the *ability* to determine..." while indicating in paragraph 154 that "the ability to take control" does not translate in having control at the present time.

**Question 4**

**Assuming that control is used as the basis for determining the composition of a group reporting entity, do you agree that:**

**(a) control should be defined at the conceptual level?**

**(b) the definition of control should refer to both power and benefits?**

**If not, why? For example, do you have an alternative proposed definition of control?**

17. See our response to Question 3.
18. We agree that there should be a basic definition of control defined at the conceptual level and that it should refer to both power and benefits.
19. Additional guidance may then be provided at the standards level to give direction on how to implement this definition at standards level.
20. The link to the Consolidation project is important as an example of how the IASB should ensure that any proposed definition works in practice. Until there is sufficient evidence of this, we suggest the IASB consider deferring issuance of the revised Standard on Consolidation. We believe that EFRAG should make this link to the Consolidation project explicit in its Comment Letter.

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**Question to constituents**

The DP assumes that control is something an entity either does have or does not have. Yet many jurisdictions have legislation or regulations that protect minority interests to varying degrees, and the effect of this is that there are more restrictions on what a 51% shareholder can do with its investment than on what a, say, 90% shareholder can do.

Some EFRAG members think the discussion in the DP—and eventually in the revised Framework—would be richer if it discussed this in terms of its control definition. (For example, one possible way of discussing the issue might be to say that, although the control definition requires the controller to have a power to direct the financing and operating policies of the controlled entity, the definition does not require the controller to have absolute power to do whatever it wanted.)

Do you think this matter should be addressed in the Framework and, if you do, what do you think it should say and why?

21. We think this matter should be addressed.

**Question 5**

**Do you agree that the composition of a group reporting entity should be based on control? If not, why? For example, if you consider that another basis should be used, which basis do you propose and why?**

22. See our response to Question 3. Like EFRAG, we do not agree that the composition of a group reporting entity should be based on control alone.

**Question 6**

**Assuming that control is used as the basis for determining the composition of a group reporting entity, do you agree that the controlling entity model should be used as the primary basis for determining the composition of a group entity? If not, why?**

23. Yes we agree with the exception mentioned in our response to Question 3. Like EFRAG, we do not agree that it should be assumed that control is used as the basis for determining the composition of a group reporting entity.

**Question 7**

**Do you agree that the common control model should be used in some circumstances only? If not, why? For example, would you limit the composition of a group reporting entity to the controlling entity model only? Or would you widen the use of the common control model? If you support the use of the common control model, at least in some circumstances, do you regard it as an exception to (or substitute for) the controlling entity model in those circumstances, or is it a distinct approach in its own right? Please provide reasons for your responses.**

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24. We agree that there is a need to allow preparing “group” financial statements in certain circumstances not captured by the controlling entity model. It would be appropriate to clearly distinguish these group financial statements from the ones prepared under the control model and to give them a different label such as “combined financial statements”.
25. However, we are concerned that the common control model may not capture all the structures for which we believe “group” reporting to be justified. We could see an apparent contradiction to permit a very broad definition of a reporting entity but a restrictive definition of group reporting entity.
26. In addition, we note that when entities are under common control of a family or an individual person, often no controlling entity can be determined. If there is no controlling group reporting entity, combined financial statements should not be applicable.
27. Accordingly, we suggest that the Board reconsider the basis for restricting the preparation of combined financial statements.

**Question 8**

**Do you agree that consolidated financial statements should be presented from the perspective of the group reporting entity, not from the perspective of the parent company’s shareholders? If not, why?**

28. The IASB in its Exposure Draft “An improved Conceptual Framework for Financial Reporting - Chapter 1 and Chapter 2” expresses the view that financial reporting should reflect the entity perspective rather than the perspective of the owners of the entity. We strongly support EFRAG’s view that a full debate is needed on the perspective from which financial statements should be prepared, before a conclusion can be reached at this stage of the Framework project.
29. In some standards, however, the parent company approach provides useful information to stakeholders/users of financial information (such as earnings per share). We are not convinced by the argument of the Board that because financial reports are prepared for a wide range of users, an entity perspective should be adopted. We encourage a more thorough debate on this issue.

**Question 9**

**Do you agree that consolidated financial statements provide useful information to equity investors, lenders and other capital providers? If not, why?**

30. We agree that consolidated financial statements provide useful information to the primary users of financial statements.

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**Question 10**

**Do you agree that the conceptual framework should not preclude the presentation of parent-only financial statements, provided that they are included in the same financial report as consolidated financial statements? If not, why?**

31. We agree that the conceptual framework should not preclude the presentation of parent-only financial statements as it serves a different purpose than the consolidated financial statements. We do not agree with the requirement to include parent-only financial statements in the same report as the consolidated financial statements. We believe that the current requirement that the consolidated financial statements should be available is sufficient, as long as the parent-only financial statements disclose that consolidated financial statements are also available.

**Question 11**

**With regard to the concept of control, in the context of one entity having control over another, do you agree that:**

**(a) establishing whether control exists involves assessing all the existing facts and circumstances and, therefore, that there are no single facts or circumstances that evidence that one entity has control over another entity in all cases, nor should any particular fact or circumstances—such as ownership of a majority voting interest—be a necessary condition for control to exist? If not, why?**

32. We agree with the proposal.

**(b) the concept of control should include situations in which control exists but might be temporary? If not, why?**

33. We agree with the proposal.

**(c) the control concept should not be limited to circumstances in which the entity has sufficient voting rights or other legal rights to direct the financing and operating policies of another entity, but rather should be a broad concept that encompasses economically similar circumstances? If not, why?**

34. We agree with the proposal. Control should be based on the economic reality and not only on legal rights and contracts.

**(d) in the absence of other facts and circumstances, the fact that an entity holds enough options over voting rights that, if and when exercised, would place it in control over another entity is not sufficient, in itself, to establish that the entity currently controls that other entity? If not, why?**

**Appendix: Responses to the questions in the Invitation to comment - Discussion Paper Preliminary Views on an improved Conceptual Framework for Financial Reporting: The Reporting Entity**

35. It may be more suitable to address this issue at the standard level. As mentioned in our response to Question 3, there is a need to clarify at the conceptual level whether, under the controlling model, consolidation arises when an entity controls at the present time another entity or whether it arises from the entity that has at the present time the ability to obtain control over another entity.

**(e) to satisfy the power element of the definition of control, power must be held by one entity only? In other words, do you agree that the power element is not satisfied if an entity must obtain the agreement of others to direct the financing and operating policies of another entity? If not, why?**

36. It may be more suitable to address this issue at the standard level, as it is necessary to complement the response with a description of what constitutes protective and participating rights.

**(f) having ‘significant influence’ over another entity’s financing and operating policy decisions is not sufficient to establish the existence of control of that other entity? If not, why?**

**Questions to constituents**

The majority of EFRAG members agree with the statement in (e) (ie that to satisfy the power element of the definition of control, power must be held by one entity only). In their view, ‘control’ and ‘joint control’ are very different things when viewed from the perspective of the controlling entity or entities. However, some EFRAG members would have liked the notion of joint control to be explored in the DP, particularly bearing in mind that they believe its application to certain transactions can result in information that is more useful than the application of the control notion. Do you have any comments on this issue?

37. We agree with the proposal.

**Question 12**

**Should any of the above control issues be addressed at the standards-level rather than at the concepts level? If so, which issues and why?**

38. See our response to Question 11. Only issues (a), (b), (c) should be addressed at the conceptual framework level. The other issues may be seen as further interpretations and should therefore be addressed at the standards-level.

**Question 13**

**Are there any other conceptual issues, relating either to the control concept or to some other aspect of the reporting entity concept, that are not addressed in this discussion paper and should be addressed at the concepts level? If so, which issues and why?**

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**Question for constituents**

So far, EFRAG has not identified any further conceptual issues that should be addressed in the DP. Do constituents believe there are any such issues?

39. We are not aware of other conceptual issues relating to the control concept or to some other aspect of the reporting entity concept that should be addressed at the concepts level.