



Association pour la participation des
entreprises françaises à l'harmonisation
comptable internationale



A F E P

Association Française des Entreprises Privées

**IASB
30 Cannon Street
London EC4M 6XH
United Kingdom**

Paris, September 29, 2008

Ref: Conceptual framework: the reporting entity

ACTEO, AFEP & MEDEF welcome the opportunity to comment on the IASB – FASB discussion paper introducing the reporting entity.

Our main comments on the discussion paper are as follow:

- Including a description of the reporting entity in the framework is useful and we broadly agree with the description proposed by the Board, albeit for some reservations;
- Choosing, within the entity's theory, between the entity's perspective and the parent company's perspective is not argued convincingly; we therefore cannot support the Board's decision;
- The conceptual framework should include a discussion on how and why consolidated financial statements are useful to capital providers in order to serve as a sound reference in discussing the model to retain and other related issues;
- Justifications for the choice of the control model and the rejection of the risks and rewards model are still awaited; we do not think that the discussion paper brings any valuable basis on which to draw a robust conclusion; we can nonetheless accept that progress is made at the standard's level on the basis of the control model as is being done at present;
- The decision that if control is retained control should be exclusive also needs to be fully substantiated; we believe that more analysis is needed and should be carried out before re-deliberations of ED9 are completed;

- Control should refer, as proposed, to a power and a benefit criteria; however we believe that more work is required to assess whether one criterion should have precedence on the other, to provide guidance on how to best analyse restrictions to the power criterion.

Detailed analysis and answers to the invitation for comment are included in the appendix.

We remain at your disposal should you need further clarification or background information.

Yours sincerely,

ACTEO

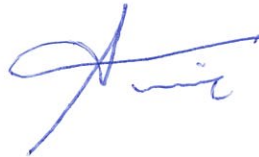
Patrice MARTEAU



Chairman

AFEP

Alexandre TESSIER



Director General

MEDEF

Agnès LEPINAY



Director of economic
and financial affairs

Section 1: The reporting entity concept

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?

We agree that what constitutes a reporting entity should not be limited to business activities that are structured as legal entities. IFRS are a set of international standards meant to apply in different legal contexts. Definitions and concepts must be robust enough to remain applicable and relevant, irrespective of the details set out in the laws of the jurisdiction where IFRS are adopted. Jurisdictions decide which entities have to comply with IFRS requirements, and hence may decide that some circumscribed areas of business activity need to report while others would be exempt from any form of requirement. We therefore agree with the arguments set out in the paper.

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 should 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?

As the reference to the reporting entity is central to the IFRS framework, we welcome the attempt of the Board to define/describe what a reporting entity is. We agree that a broad description is retained. We also believe that the link to the objective of financial reporting is relevant. However the notion of "circumscribed area of business activity" suggests active operations. A circumscribed area of business activity can be at times inactive. We believe that such circumstances should be encompassed in the proposed definition.

Section 2: Group reporting entity

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?

We cannot support the Board's conclusion because we believe that it is not appropriately justified.

Although accounting requirements in various jurisdictions have made consolidated financial statements mandatory for quite some time, we believe that a discussion at the conceptual level should start with revisiting why and how the combination of different entities in a group reporting entity provides useful information to capital providers – or identify what information would be lost if consolidated financial statements were not prepared. We believe such a starting point (probably very basic and non-controversial) would be useful guidance in discussing the model to be retained at the conceptual level, justifying why a model would not be relevant, and later in defining how that model should apply at the standard level, i.e. whether there should be exceptions to the consolidation requirement.

We understand that for efficiency reasons the Board has not thought useful to develop models that in its view carry no future. Contrary to the assertion that the Board has considered the risks and rewards model as a possible candidate, we observe that the Board reaches the decision not to retain the risks and rewards model without any sound justification. The only reason for rejection seems to be that the model does not work without significant further development. Without the effort made by the Board in the definition of the control model, one could also conclude that the control model should not be retained because more work is needed to make it robust enough. We also observe that the Board does not justify convincingly why control (including the ability to benefit) would be determinant of what should be combined and what should not. We are calling, at the conceptual level, for a sound analysis of why and how the control model is relevant, and why and how it is more relevant than the risks and rewards model. Before such an analysis is carried out, we do not believe that any valid conclusion can be drawn.

We can concur with the Board that making the necessary effort at the conceptual level is not for the time being a priority, the Board's stated preference leading to no fundamental change in the existing literature. We believe however that in such a case the Board should refrain from drawing conclusions at the conceptual level and leave the subject open for further analysis when time for doing so becomes available. In the meanwhile the IASB can work on improving its standard on consolidation on the basis of the existing control model, including as indicated in the DP, overlaps with the risks and rewards model where those overlaps appear helpful (ref to paragraphs 102 and 103 of the DP).

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?

We agree with the Board that control should be defined at the conceptual level. However we have the following reservations regarding the definition proposed:

- The definition proposed suggests that asset managers have control of the entities for which they bear stewardship responsibilities, when their remuneration is based on performance (although the discussion clearly indicates that this is not intended); in our view, the conceptual definition of control should not need be refined or restricted at the standard's level;
- The definition and the discussion surrounding the definition suggest precedence of the power criterion over the ability to benefit; no discussion in the DP indicates how this choice is justified; we believe that the opposite approach would be worthwhile exploring, in a direction such as "control is the ability to access benefits and bear risks from an entity of which no other entity has the ability to direct the financing and operating policies";
- We believe necessary to analyse the implications of restrictions to the exercise of exclusive power in situations where notwithstanding restrictions control continue to be exercised. Indeed legal frameworks may limit the extent to which the controlling entity may benefit, in view for example of the safeguard of minority interests or of other external capital provider. It will be necessary at the standard's level to define where control starts and where control ends, for example how veto rights should be analysed. Guidance at the conceptual level would be helpful. The analysis we call for in the first paragraph of our answer to question 3 should provide the necessary reference;
- The conclusion reached that control is necessary exclusive needs to be thoroughly investigated and justified.

In addition to the above reservations, we observe that the Board is actively working on a revised standard on consolidation in which the definition of control plays a key role. We believe that the IASB's thinking in that project provides valuable input for strengthening the control definition. As a result we recommend that the two projects interact as much as possible while they are being developed.

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?

As indicated in our answer to question 3, we can agree that for the time being the composition of a group reporting entity remains based on control.

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?

Assuming that control is used as the basis for determining the composition of a group reporting entity, we agree that the controlling entity model should be used as the primary basis for determining the composition of a group 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.

We believe that the common control model is welcome in situations where the controlling entity model would not be applicable and where combined financial statements would be useful to capital providers. We see that model more as an extension of the control model than as an exception to it. Defining when the common control model could – or should – apply should flow from the analysis we have called for in the first part of our answer to question 3.

Section 3: Parent entity financial reporting

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?

For several years the Board has been pushing forward the entity perspective without ever providing a solid rationale for it. It all started with the 2004 improvement project when it was decided that minority interest should be part of equity. At the time the justification was the desirable consistency with the framework definition of a liability. The issue has been raised more than once since then, and more especially within the conceptual framework project, without the Board developing convincing arguments. Lately the justification seems to be that the entity perspective is the perspective which better suits the needs of all capital providers by opposition to the investors in the parent company. We however do not believe that this argument works well. There exists the same difference of perspective among lenders than there does among shareholders, i.e. those that have interests in a subsidiary and those that have interests in the parent company. We believe that the capital providers most interested in the consolidated statements of a group are the capital providers to the parent company. The subsidiary accounts, including information on related party transactions, will be of much greater use to the other capital providers.

We are all the more concerned by the position taken by the Board that the staff has declined to develop the appropriate arguments on the issue, stating that there were not in a position to clearly articulate all consequences of the choice of the entity's perspective at the conceptual level (London, April 2008 IASB Board meeting). We must admit that we are in the same position as the IASB's staff. We therefore believe that the conclusion should remain pending until the appropriate analysis is carried out.

Question 9

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

We agree that consolidated financial statements provide useful information to capital providers. However as indicated in our answer to question 3, we believe that the Board should have developed why and how this information is useful.

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?

We support the IASB's view that the conceptual framework should not preclude parent-only financial statements from being presented. We believe that parent-only financial statements can provide useful information in addition to consolidated financial statements. As a result, we are opposed to any statement that consolidated financial statements are self-sufficient with the current disclosures. Indeed we believe that capital providers of the parent company need at least information such as the valuation of the investments of the parent in the subsidiaries, the extent and characteristics of the liabilities which are born by the parent company, related party transactions from the perspective of the parent only..., information which is today included in the parent-only financial statements.

We believe that determining why and how parent-only financial statements are useful, whether they have an information value in their own right, requires a substantial and dedicated work, none that can be valuably concluded upon at the conceptual level. We therefore welcome the view that further work at the standard's level is required.

Section 4: Control issues

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 fact or circumstance that evidence that one entity has control over another entity in all cases, nor should any particular fact or circumstance – such as ownership of a majority voting interest – be a necessary condition for control to exist? If not, why?***

We agree.

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

We agree. However we wonder whether consolidated financial statements are likely to bring useful information in all circumstances where control is temporary. We believe that this is an issue to be explored at the standard's level.

- 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?***

We agree.

- 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?***

We fully agree with the analysis in paragraphs 155 – 156.

- 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?***

Statement e) above contradicts statement a). Shared power is power and a fact and circumstance analysis is needed to determine whether the limitations involved preclude control. That issue has also to be analysed in the light of conclusions reached in c) and d) above, d) in particular shedding new light on the issue of control.

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. It is not clear to us that situations of shared power bring more restrictive limitations to the entity's power than those that the legal framework of a jurisdiction can provide to protect minority interest rights. 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.

Such an analysis could also give a valuable insight in order to better assess the substance of protective rights. We indeed believe that the present notion of protective rights is much too restrained.

- 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?***

We agree.

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?

All of the issues raised in question 11 will necessarily be addressed at the standards level. However guidance, either general or specific, should be provided at the conceptual level if conclusions at the standard's level are to be expected robust, consistent and best serving users' needs.

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?

Except for what we have suggested in our answers to questions 3 and 11 e), we see none.

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