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Sir David Tweedie  
Chairman  
International Accounting Standards Board  
30 Cannon Street  
London EC4M 6XH  
United Kingdom

Dear Sir David,

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, I appreciate the opportunity to comment on the Discussion Paper *Preliminary Views on an improved Conceptual Framework for Financial Reporting – the Reporting Entity* (May 2008). Principal authors of this comment letter were Peter Geyer, Roland Nessmann, and Alfred Wagenhofer.

### **General comments**

We would like to point out that we welcome the discussion of the issues raised in the paper. The recent developments in accounting and financial reporting practice showed certain conceptual gaps and certain inconsistencies between various accounting standards.

The current framework mentions the reporting entity only in passing (para 8: “A reporting entity is an entity for which there are users who rely on the financial statements as their major source of financial information about the entity.”). The definition gives too much leeway for interpretation and is not sufficient as a general guidance.

The initiative to define the reporting entity in the conceptual framework closes certain gaps and has the potential to improve the standard setting for the reporting entity issues in the long run. The concep-

tual framework can, therefore, provide a sound basis for the development of relevant and consistent standards in this area.

The discussion paper mainly contains proposals for rules within the conceptual framework. Such rules shall in general focus on principles. Peculiarities and exceptions should not be part of the framework, but be regulated at the level of the financial reporting standards, where deemed necessary.

## Specific comments

**Q1.** *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?*

Yes, we agree. General purpose financial reports should not be restricted to legal entities. Although the identification of assets and liabilities of business activities that are structured in form of legal entities, may be easier in compare with to other structures like sole proprietorships, unincorporated branches, special types of corporations etc, even those other structures should be able to constitute a reporting entity for general purpose financial reports. For activities that do not have their own legal existence, their peculiarities will need to be taken into consideration and practical difficulties may occur. However, these peculiarities and difficulties can be addressed at the standards level in order to achieve a reporting level comparable to that of legal entities.

**Q2.** *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?*

Yes, we agree with a broad description. The definition of a reporting entity as a “circumscribed area of business activity” is still very general but implies that there are or will be more specific definitions elsewhere. While we believe that the reporting entity is appropriately defined in the discussion paper, we would suggest including guidance on what basis specifications will be developed in individual standards.

The focus on the interests of equity investors, lenders and other capital providers follows directly from the discussion of general purpose financial reporting in Chapter 1 of the framework.

**Q3.** *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?*

Yes, we agree.

The risks and rewards model in general seems to be too complex for determination of reporting entities and even impracticable to act as a robust basis for determining the composition of a group reporting entity. Risk and rewards are however relevant for the 'controlling entity model'. They can serve as indicators in the controlling entity model (e.g. context of SPEs).

**Q4.** *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?*

Yes, we agree with both (a) and (b). The definition of control, including the references on power and benefits at the conceptual level is desirable, as the conceptual framework forms the basis for all standards. A definition of control (although in general terms) will help to avoid inconsistencies between standards and support compact standard setting in the long run.

**Q5.** *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?*

Yes, we agree. Most of the jurisdictions worldwide are using the control approach (or a closely related approach) for determining reporting groups. The practicability of the control approach is evident. The definition of control, as outlined under question 4, should occur at the conceptual level.

**Q6.** *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?*

Yes, we agree.

**Q7.** *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.*

Yes, we agree that the common control concept should be used in some circumstances only. Its application should be limited to rare cases like the example outlined in paragraph 85. The common control approach should not represent an exception to (or substitute for) the controlling entity model but a distinct approach in its own right.

**Q8.** *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?*

Yes; we agree. Over the recent decades, in most jurisdictions we have seen certain shifts from more or less "parent company" approaches towards the "group reporting entity" approach. The "group reporting entity" approach better reflects the group activities in its entirety whilst the parent company approach offers less information.

Consistent with the focus of general purpose financial statements on the interests of present and potential equity investors, lenders and other capital providers, non-controlling equity investors should be provided with the same relevant information concerning their investments within the statements of shareholders equity as controlling equity investors.

When applying the group reporting entity approach, certain issues will likely come up, which need to be addressed at the standards level. Such issues are the presentation of results from transactions between controlling and non-controlling equity investors and the allocation and measurement of goodwill in business combinations.

**Q9.** *Do you agree that consolidated financial statements provide useful information to equity investors, lenders and other capital providers? If not, why?*

Yes, we agree.

**Q10.** *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?*

No, we disagree with the proposed requirement that parent-only financial statements should be included in the same financial report as consolidated financial statements. As discussed in the discussion paper, many countries have legal requirements to prepare parent-only financial statements. It may be difficult to sufficiently differentiate group and parent-only information in the same financial report, and it may be confusing to do so.

Another issue is that legal requirements may be such that parent-only statements must be prepared under IFRS or under national GAAP. It is not clear if the discussion paper refers only to IFRS parent-only financial statements (we believe it does) or to parent-only financial statements in general.

Therefore, we suggest requiring cross-referencing: the parent-only financial statements should contain a note that the entity is a parent and prepares consolidated financial statements, and where these statements are available. And the consolidated financial statements should contain a note to indicate that the parent company – and also subsidiaries – prepare parent-only (individual) financial statements and the source where they are available. This could avoid confusion, but include sufficient transparency about complementary information that often is of interest to a minority of users only.

**Q11.** *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?*

Yes, we agree.

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

In principle, yes. However, we suggest shifting discussion of that situation from the conceptual framework level to the standards level.

In any case, we suggest including a sufficient basis for the discussion of this situation. For example, there appear to be certain similarities to the situation of disposal groups.

*(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?*

Yes, 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?*

In principle, yes. However, we suggest shifting discussion of that situation from the conceptual framework level to the standards level. We can conceive many other special situations that are not directly addressed in the discussion paper, but appear to be similar to that raised. That is, we suggest sticking to principles in the discussion paper.

In any case, we suggest including a sufficient basis for the discussion of this situation.

*(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?*

Yes, we agree that power must be held by one entity only.

*(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?*

Yes, we agree. Significant influence is a necessary condition, but certainly not a sufficient condition for the existence of control.

**Q12.** *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?*

As noted in our answers to Q11. we believe the issues (b) and (d) should be dealt with at the standards level.

**Q13.** *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?*

We do not see other conceptual issues not dealt with in the discussion paper.

Please do not hesitate to contact me if you wish to discuss any aspect of our comment letter in more detail.

Kind regards,

Romuald Bertl  
Chairman