



M A Z A R S

International Accounting Standards Board
30 Cannon Street
London EC4M 6XH
United Kingdom

20 March 2009

Dear Sir / Madam,

Re: Comments on IASB Exposure Draft ED 10 Consolidated Financial Statements

Mazars welcomes the opportunity to comment on the Exposure Draft ED10 Consolidated Financial Statements.

We appreciate the efforts made by the IASB to address some urgent issues that have arisen during the recent financial crisis and the consequent necessity to answer as fast as possible to the need for actions.

This project's objectives are to improve disclosure requirements about consolidated and unconsolidated entities and to improve the definition of control so that a control model can be applied to all entities.

We globally support the additional disclosures required by the project, as there is an urgent need for more transparency, even though we believe that the main objective should be made clearer. The entity should be able to decide the level of detail of the information to be provided to meet the objectives.

We also support the IASB's objective to develop a revised standard based upon a unique definition of control, as we believe that a single principle of control that can be applied to all entities would be a conceptual improvement on the current guidance.

However, we have serious concerns about the proposed new definition of control as:

1. Contrary to what is implied in the introduction (§ 3), we believe that the current application of IAS 27 and SIC 12 is globally satisfactory.

In this respect, we found little evidence of practical problems encountered in implementing the requirements of IAS 27 or SIC 12 that would justify modifying the underlying consolidation principle without delay.

2. We therefore believe that there is no need to change the consolidation principles urgently (even though we acknowledge that the guidance could be improved).

We also note that normal due process has not been followed since the Board moved directly to an exposure draft without previously providing a discussion paper on the topic. In addition, the comment period is 90 days instead of the usual 120-day period.

We realise that the Board has accelerated the project in response to the global financial crisis. However, control is a significant issue and debate on the issue should not be rushed.

3. In addition, the project is not led jointly with the FASB, and will therefore not result in greater convergence with US GAAP.

We believe a joint project addressing the current issues in both US GAAP and IFRS would result in a permanent global solution, rather than a solution that is likely to change again as US GAAP and IFRS converge in the future.

4. Above all, we are not convinced that ED 10 as drafted represents an improvement on existing IFRSs.

In practice, we think the consolidation principles in existing IFRSs are preferable to the one being proposed in the ED since the current requirements work reasonably well in practice and there is not an urgent need for improvement.

5. The project does not demonstrate that it responds to users' information needs in terms of consolidation.

Beyond the question of having a robust unique definition of control, the practical question is whether consolidated financial statements will include the "right entities" (i.e. the right entities being consolidated and the right ones remaining off-balance sheet).

In this respect, the public's expectations would be that more entities would be consolidated, rather than less, whereas we are afraid that the project would allow more structuring opportunities.

6. Furthermore, we are not sure that the consequences of other projects have properly been taken into account. More specifically, there is an obvious need to work simultaneously on consolidation and derecognition, as those two project are inter related.
7. Also, we doubt that the project is "workable" as it is, considering the lack of clarity in the guidance and the resulting risk of inconsistent application.
8. Lastly, this project has been presented as improving and unifying the definition of control, and has not been presented as a significant change to present practice albeit there has been no field testing.

We believe that the proposal, which potentially could lead to changes in the scope of consolidation of entities, should not be implemented until extensive field-testing amongst preparers has been carried out which clearly demonstrates the advantages of ED 10 over current IFRSs for financial reporting purposes.

Overall, we believe that a substantial change such as a change in the consolidation principle should only be made if it provides users with more useful information. We are not convinced that the new consolidation principle will be more appropriate in terms of those users needs.

As a consequence, we believe that the IASB should split the project in two distinct parts:

- A first part, the implementation of the proposed disclosures, that needs an urgent answer, and that should be finalised in the short-term, subject to some clarifications,
- A second part, involving the implementation of a single, universally-applied consolidation principle, which should be conducted in cooperation with the FASB, would assure the coordination with the other IASB projects (like the "derecognition" project for example) and which could be properly supported by an appropriate field test.

As the current requirements work reasonably well in practice, and therefore are not in an urgent need of improvement, this second part would benefit from additional time.

We would be pleased to discuss our comments with you and remain at your disposal should you require further clarification or additional information. Would you have any request regarding the above comments, please do not hesitate to contact Michel Barbet-Massin (+33 1 49 97 62 27).

Yours faithfully



Michel Barbet-Massin
Head of Financial Reporting Technical Support

Question 1

Do you think that the proposed control definition could be applied to all entities within the scope of IAS 27 and SIC 12?

We support the objective of having a single consolidation principle, which would encompass the scope of both IAS 27 and SIC 12. However, we consider that any change to the control definition should only be made if it provides users with more useful information about the group.

In practice, applying the definition of control, as it is proposed in the project, to structured entities will prove difficult as the “power” component of the control definition is particularly difficult to assess in the case of structured entities.

Firstly, we are not convinced that there are always decisions that need to be made in the case of structured entities, whereas the project seems to assume that there are no entities that are totally “auto-piloted”.

Secondly, power could be shared between different parties in order to reach a particular accounting result, namely that no one consolidates the structured entity. We therefore see some merits in the alternative view expressed in AV8.

Thirdly, the project does not distinguish between decisions that are substantive and those which may not be substantive, leading us to believe that the project as it is would offer a lot of structuring opportunities.

In other words, the proposed principle focuses on the ability to direct the activities that affect the variability of the returns, regardless of whether that variability is substantive, whether those returns are substantive, and whether the ability to direct is substantive. We think the result is that sometimes the focus of the ED’s requirements would be on non-substantive aspects of an entity’s relationship with a structured entity. In such a case, ED 10 would require consolidation of a structured entity but SIC-12 may not.

As a consequence, we believe that only extensive field testing would be able to demonstrate that the proposed control definition is appropriate and “workable”.

Question 2

Is the control principle as articulated in the ED an appropriate basis for consolidation?

The control principle is articulated differently between entities where the determination of strategic operating and financing policies are important (non-structured entities, or “traditional” entities) and structured entities.

Whereas the project’s objective was to replace IAS 27 and SIC 12, it appears to have put together different guidance for the different types of entities covered, without truly unifying the control definition.

In other words, the project appears more like a juxtaposition of two different approaches than as the application of a new consistent and clear principle. Such a solution may be considered as a pragmatic one. However, in such a case, we are favoring a mere inclusion of SIC 12 principles into IAS 27 without changing IAS 27 control definition.

We believe that the guidance should not be distinguished between structured entities and other entities, but rather that different examples and indicators of control should be given.

Question 3

Are the requirements and guidance regarding the assessment of control sufficient to enable the consistent application of the control definition? If not, why not? What additional guidance is needed or what guidance should be removed?

In order to have a consistent application of the control definition, it is necessary that the guidance be clear, unambiguous, and also internally consistent.

In this respect; we believe that the distinction between having the power to direct and having actually made use of the power should be clarified.

Other aspects of the guidance would also need clarification:

- It is not clear whether returns need to be potentially positive and negative. The example in §B8 suggests that returns must be potentially negative returns (i.e. downside). We believe that this point should be clarified. This also raises the question of the level of the potentially negative side, for example for options.

- Also, regarding the guidance on the distinction between an agent and a principal, we are wondering whether variable fees (that are commensurate with the service performed, i.e. market based variable fees) obtained by a fund manager should be considered as returns in the analysis or not.
- It is not clear whether “legal supervision” (§ 25) should be read as carrying over the guidance of IAS 27.21, and we therefore suggest that the Board specifies how this term should be interpreted.
- Introduction of guidance regarding protective rights is positive, but we suggest extending the guidance to situations where participating rights are substantive.
- The ED states that there can be circumstances in which an entity is not controlled by any entity at all. However, we regret that this concept can only be found in the introduction (§ 11) and is not further explained.

Overall, in terms of structuring the guidance, we believe it would be preferable to better distinguish between what should be contained in the standard itself, what is contained implementation guidance and what is the Board's rationale (i.e. the basis for conclusion).

Question 4

Do you agree with the Board's proposals regarding options and convertible instruments when assessing control on an entity? If not, please describe in what situations, if any, you think that options or convertible instruments would give the option holder the power to direct the activities of an entity?

We believe the guidance on options should preferably be in the application guidance rather than in the basis for conclusion (§ BC74-BC87).

Overall, we find the guidance confusing and not helpful. If the Board's conclusion is that options would only rarely transfer the control, then it would be preferable to say so, together with providing examples where options transfer the control.

However, we are not convinced by the rationale and therefore are sympathetic with the views expressed in AV3-AV6 and believe that the current treatment is more adequate.

Under current IAS 27, options would rarely be taken into account when determining the percentage of interest (§ IG5-IG7). Paragraph B19 of the project always considers that options cannot be taken into account, which does not seem consistent with the Board's conclusion in BC 85 that the option holder has a controlling interest.

In addition, given that returns also include costs savings and returns that are not available to non-controlling interest, the Board's conclusion in BC 86 stating that fair value options fail the second part of the control definition may not always be true.

Question 5

Do you agree with the Board's proposals for situations in which a party holds voting rights both directly and on behalf of other parties as an agent? If not, please describe the circumstances in which the proposals would lead to an inappropriate consolidation outcome.

We agree with the proposal and related guidance that voting rights held directly and on behalf of other parties needs to be considered together in order to determine whether the reporting entity controls that other entity.

We believe that the guidance should be further developed to better define whether an entity is acting as an agent or as a principal, taking into consideration the additional guidance provided to IAS 18 in the 2008 annual improvement project.

In addition, further guidance should be provided for fund managers, acting in a fiduciary capacity, that have variable fees (commensurate with the services provided). At this stage, it is not entirely clear under what circumstances the fund manager that also has invested directly in funds which it manages would be obliged to consolidate.

Question 6

Do you agree with the definition of a structured entity in paragraph 30 of the draft IFRS? If not, how would you describe or define such an entity?

We do not understand the need to give a specific definition to a structured entity as the objective of this project is to provide a single definition of control that can be applied to all types of entities.

In effect, providing such a specific definition of a structured entity has led to develop two sets of criteria depending on the characteristic of the entity, whereas the only use of the definition is to determine the entities subject to specific disclosures.

In addition, the only examples provided are within the financial services sector. It would be beneficial to also provide other examples.

Last, we would favor having a positive definition, rather than a definition by default.

Question 7

Are the requirements and guidance regarding the assessment of control of a structured entity in paragraphs 30–38 of the draft IFRS sufficient to enable consistent application of the control definition?

We are not entirely convinced the control definition is robust enough and as a result we believe the project suffers from the following weaknesses:

- The assessment of control in the case of structured entities should not be separated from “normal” entities since that calls into question the fact that there is one definition of control, applicable in all cases. Otherwise, we support keeping IAS 27 and SIC 12 definitions.
- The project leaves room for structuring opportunities, through dispatching control between different parties so that no one is deemed to control the entity, or through disguising control.
- The project assumes that no entity is completely auto-piloted and we are not sure whether this assumption is correct.

It is also not clear from the project whether there is a presumption of control for a party that would have the highest returns.

According to § 33, “a reporting entity is likely to have power to direct the activities of a structured entity if it is exposed to the variability of returns that are potentially significant to the structured entity and the reporting entity’s exposure is more than that of any other party” whereas BC 119 explicitly states that “the Board considered whether (and decided not) to include a rebuttable presumption of control of a structured entity when a reporting entity has rights to a particular level of returns”.

The overall effect of these two paragraphs is that the conclusion is unclear and this point should be clarified.

Question 8

Should the IFRS on consolidated financial statements include risks and rewards ‘fall back’ test? If so, what level of variability of returns should be the basis for the test and why? Please state how you would calculate the variability of returns and why you believe it is appropriate to have an exception to the principle that consolidation is on the basis of control.

As indicated above, we are concerned that an entity that clearly and obviously has the majority of the risks and rewards of a structured entity could easily avoid consolidation by circumventing the power criterion, which is essentially the view expressed by Mr. Smith in AV9-AV12.

However, even though we have serious reservations about the project as it is, we believe that the risk and rewards fall back test is not consistent with the approach taken by the Board. To do so would defeat the purpose of the exposure draft, i.e. to have a single definition of control for all entities.

Question 9

Do the proposed disclosure requirements described in paragraph 23 provide decision-useful information? Please identify any disclosure requirements that you think should be removed from, or added to, the draft IFRS.

We broadly agree with the disclosure requirements. However, we believe that it should be made clearer that the disclosure requirements are subject to the general principle set out in paragraph B31 that states that the entity is able to decide the level of detail of the information to be provided to meet the objectives.

In effect, having detailed information related to a list of unconsolidated entities may not provide useful information.

Although not directly derived from B31, we believe that this principle would lead an entity to adjust the level of detail based upon both the amounts involved (i.e. the risk exposure) and the degree of involvement.

Regarding §B33-B34, we believe that information in aggregate about consolidated and non consolidated entities has little value. Instead, it would be preferable disclosing separate information for major entities (either consolidated or non consolidated) where judgment was significant.

Question 10

Do you think that reporting entities will, or should, have available the information to meet the disclosure requirements? Please identify those requirements with which you believe it will be difficult for reporting entities to comply, or that are likely to impose significant costs on reporting entities.

We see no basis for requiring two years of comparative information (§ 42).

Considering the fact that information required by IAS 28 for disclosures relating to associates may prove difficult to obtain, information may not be easy to collect from non-controlled structured entities.

Question 11

Do you think that reputational risk is an appropriate basis for consolidation? If so, please describe how it meets the definition of control and how such a basis of consolidation might work in practice.

Do you think that the proposed disclosures in paragraph B47 are sufficient? If not, how should they be enhanced?

We agree with the Board that the existence of reputational risk is not in itself an appropriate basis for consolidation. We consider the proposed disclosure is sufficient when support has effectively been provided to the structured entities in the absence of a constructive obligation to do so.

Question 12

Do you think that the Board should consider the definition of significant influence and the use of the equity method with a view to developing proposals as part of a separate project that might address the concerns raised relating to IAS 28?

We are not aware of any significant application issues regarding the equity method and therefore see no reason to take on a new project. This said, some aspects of IAS 28 could be dealt with through the annual improvement process, notably to clarify the consequences of IFRS 3R on IAS 28.

In any case, we believe that any large revision to the equity method should follow a proper due process.

In addition, whatever the theoretical problems related to equity accounting might be, any change should take into account the usefulness for the users of financial statements.

In this regard, we believe equity investments are not comparable to investments in AFS, where the investor is passive.