Bundesverband deutscher Banken

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

13 September 2002
H 3.9 - Sü/To

Exposure Draft of Proposed Improvements to International Accounting Standards

Dear Madam, dear Sir,

We welcome the opportunity to comment on the proposed improvements to International Accounting Standards (IAS). Our comments focus on those IAS which are of particular relevance to banks. We should like to begin by making some general observations:

We warmly endorse the IASB's objective of developing accounting principles which are coherent and free of alternatives. Against this background, we regard the IASB's improvement project as an important and useful approach to furthering global convergence, eliminating alternatives and improving the overall quality of the standards.

Clear, unequivocal rules are a prerequisite for high-quality standards. In our view, the increasingly casuistic nature of some rules are putting this principle at risk. Casuistic rules can give rise to contradictions. Certain individual standards contain differing rules on the treatment of revaluations, for example. For available-for-sale financial instruments, the recently published ED IAS 39.119 envisages that impairment losses recognised in previous profit and loss accounts shall not be subsequently reversed through the income statement. In contrast, ED IAS 16.37 (property, plant and equipment) and IAS 38.76 (intangible assets) expressly require a reversal of a previous revaluation decrease to be recognised as income. In addition, formulating rules on specific, individual sets of circumstances rather than setting out broad principles results in the IAS becoming excessively cumbersome with undesirable scope for discretionary leeway. Take, for

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example, the provisions in ED IAS 1.60-64 listing individual circumstances which need not be considered in the financial statements if they have occurred after the balance sheet date. It would be more appropriate, in our view, to formulate a general accounting principle stating that events occurring after the balance sheet date are not to be considered in the financial statements. Individual examples could then be supplied to explain and illustrate this basic rule.

Furthermore, certain specific issues which may be regarded as marginal to the overall objectives of the project are regulated either contrary to the existing approach or in an excessive amount of detail (e.g. the new rules on earnings per share, certain disclosure requirements regarding related parties, subsidiaries and associates). This runs counter to the IASB's objective of setting minimum standards and, in some cases, would require extensive modifications and adjustments in preparing financial statements without offering users any discernible additional benefit.

It is far from clear that it will be possible to implement the new rules by 1 January 2003. We understand the consultation process to mean that the proposed changes are not yet final. Only when the rules have been finally adopted by the IASB after the end of the consultation phase does it make sense for companies to start the implementation process.

We should also like to point out that the period of time between the publication of a standard or interpretation and the date of its initial application is constantly getting shorter. Normally, however, at least one year is needed to carry out the IT adjustments, programming and processing modifications necessary to implement a new standard. Furthermore, large companies require considerable time and manpower to disseminate information on a new standard throughout the entity. With this in mind, and assuming the standards are adopted on schedule, we recommend that the revised standards should enter into force on 1 January 2004.

We also ask the IASB to bear in mind that in the EU, many companies, including small enterprises, will be required to prepare their consolidated financial statements in accordance with IAS from 2005 at the latest. Against this background, greater importance should be attached to cost-benefit considerations from the outset when standards are reviewed.

Our comments on specific standards are as follows:

IAS 1 Presentation of financial statements

Question 1:

Do you agree with the proposed approach regarding departure from a requirement of an International Financial Reporting Standard or an Interpretation of an International Financial Reporting Standard to achieve a fair presentation (see proposed paragraphs 13-16)?

Reply:

No, we do not agree with this approach regarding departure from individual standards.

Under ED IAS 1.11, an entity's financial statements will only comply with IFRS if all the requirements of each applicable standard and interpretation are met.

Under IAS 1.13, it was necessary to depart from the requirements of a standard or interpretation if the management concluded that compliance would conflict with the objective of the framework, namely to provide a fair presentation of the actual financial position, and therefore be misleading. ED IAS 1.13 adds the proviso that national law must allow, or at least not prohibit, such a departure. Should national law prohibit this departure, the balance sheet and income statement may, under ED IAS 1.15, only depart from requirements to the extent national law allows.

In our view, national regulations cannot be allowed to dictate how IAS financial statements are prepared. In extreme cases, this would mean entities whose IAS financial statements were used in several countries would have to prepare different statements to comply with the laws of different jurisdictions.

According to IAS 1.14, "The existence of conflicting national requirements is not, in itself, sufficient to justify a departure in financial statements prepared using International Accounting Standards". This requirement should continue to be respected and a national regulation should not result in modifications to the international rules of the IFRS. We advocate an obligation to depart from requirements – irrespective of national regulations – in the extremely rare cases where compliance with a standard would produce a misleading picture. We are therefore in favour of retaining the existing wording in IAS 1.14.

The wording of ED IAS 1.14 (d) is unclear, in our view. Irrespective of this point, we consider the requirement to state, <u>for each item</u>, the fictitious amount that would have resulted from literal compliance to be excessive and impracticable. We suggest instead a rewording on the basis of IAS 1.13(d) to the effect that it is sufficient to explain the departure from a requirement by describing its potential impact on the balance sheet, income statement, equity and cash flows.

Question 2:
Do you agree with prohibiting the presentation of items of income and expense as "extraordinary items" in the income statement and the notes (see proposed paragraphs 78 and 79)?

Reply:
In principle, we welcome a restriction on the presentation of "extraordinary items". However, we believe it would be more useful to deal with this issue in the upcoming Reporting Performance Project rather than seeking at this stage to find a short-term solution to a single aspect of performance presentation.

We should like to point out that net income is to be used as a forecasting tool. Thus, it will always be necessary to separate extraordinary and one-off items from the results by some means or other. Eliminating such a position altogether will therefore not serve a useful purpose, in our view. Suitable methods of presenting extraordinary and/or one-off income items should be discussed in the above-mentioned project.

Question 3:
Do you agree that a long-term financial liability due to be settled within twelve months of the balance sheet date should be classified as a current liability, even if an agreement to refinance, or to reschedule payments, on a long-term basis is completed after the balance sheet date and before the financial statements are authorised for issue (see proposed paragraph 60)?

Reply:
Yes, we agree with the proposed procedure. If the agreement to refinance or reschedule payments is made after the balance sheet date, this should not be taken into account in the financial statements for the reporting period.

However, we criticise the casuistic rules on specific, individual cases of factors influencing values in paragraphs 60-64 (questions 3 and 4). We propose setting out a clear accounting principle stating that events occurring after the balance sheet date shall not be taken into account in the annual financial statements.

As far as banks are concerned, we consider this question irrelevant inasmuch as, under IAS 1.53 / IAS 30.18, assets and liabilities are presented in order of their liquidity, so that a differentiation between current and non-current does not apply.

Question 4:

Do you agree that:

(a) a long-term financial liability that is payable on demand because the entity breached a condition of its loan agreement should be classified as current at the balance sheet date, even if the lender has agreed after the balance sheet date, and before the financial statements are authorised for issue, not to demand payment as a consequence of the breach (see proposed paragraph 62)?

(b) If a lender was entitled to demand immediate repayment of a loan because the entity breached a condition of its loan agreement, but agreed by the balance sheet date to provide a period of grace within which the entity can rectify the breach and during that time the lender cannot demand immediate repayment, the liability is classified as non-current if it is due for settlement, without that breach of the loan agreement, at least twelve months after the balance sheet date and:

(i) the entity rectifies the breach within the period of grace; or

(ii) when the financial statements are authorised for issue, the period of grace is incomplete and it is probable that the breach will be rectified (see proposed paragraphs 63 and 64)?

Reply:

See reply to question 3.

(a) The information that the lender is not taking action as a result of the breach is a factor influencing the value, which should not be taken into account in the financial statements for the reporting period.

(b) (i) Yes, we agree with the proposed rule.

(b) (ii) Yes, we agree with the proposed rule.

Question 5:

Do you agree that an entity should disclose the judgements made by management in applying the accounting policies that have the most significant effect on the amounts of items recognised in the financial statements (see proposed paragraphs 108 and 109)?

Reply:
Yes, we agree, in principle, with the requirement to indicate the major judgements made by the management in selecting and applying accounting and valuation methods. However, we consider that a general qualitative description should be sufficient to fulfil these disclosure requirements.

Question 6:
Do you agree that an entity should disclose key assumptions about the future, and other sources of measurement uncertainty, that have a significant risk of causing a material adjustment to the carrying amounts of assets and liabilities within the next financial year (see proposed paragraphs 110-115)?

Reply:
There is some overlap between ED IAS 1.110 ff. and ED IAS 1.7. Banks, in particular – as required under IAS 32.42 ff – disclose extensive information on risk management and risk controlling, by quoting value-at-risk figures, for example. This disclosure is usually in the form of a risk report, which – at least in Germany – is included in the management report. We advocate an overall, combined presentation of risk management policies, uncertainties and a forecast. It should be left to the company to decide whether to incorporate this information in the management report or in the notes. Repetition and the fragmentation of related information run counter to the aim of making financial statements clear and understandable, in our view.

We reject the rules in ED IAS 1.112. Rather than arbitrary and impracticable detailed rules and simulations, we are in favour of a comprehensive and consistent presentation of risk – on the basis of a value-at-risk approach, for example.

In this context, we recommend incorporating the management report, including the risk report, in the scope of the IFRS. ED IAS 1.9 would then need to be adjusted.

Additional remarks
Mandatory presentation in the balance sheet or income statement of all the items mentioned in ED IAS 1.65 and ED IAS 1.76 respectively has not proved effective in practice. The principle of materiality should be applied to decide whether certain information should be included in the balance sheet/income statement or in the notes.

IAS 8 Accounting Policies, Changes in Accounting Estimates and Errors

Question 1:

Do you agree that the allowed alternative treatment should be eliminated for voluntary changes in accounting policies and corrections of errors, meaning that those changes and corrections should be accounted for retrospectively as if the new accounting policy had always been in use or the error had never occurred (see paragraphs 20, 21, 32 and 33)?

Reply:

(a) Voluntary changes in accounting policies

In principle, we welcome the proposal to eliminate the allowed alternative treatment for voluntary changes in accounting policies. The effects of the change must not be allowed to influence the results of the reporting period, but should be accounted for retrospectively.

In order to ensure comparability and consistency of financial statements over a period of time, however, voluntary changes in accounting policies should be limited to rare exceptional cases (principle of consistency). In particular, a change in accounting policy should not be allowed if the only reason behind the change is a more advantageous presentation of performance.

We suggest clarifying in ED IAS 8.9 that changes in accounting methods and/or policies may only be implemented very rarely and under particular circumstances. We assume that the principle of materiality applies to retrospective changes in value and would suggest this aspect be explicitly included in the provisions of ED IAS 8.20.

(b) Corrections of errors

The draft standard envisages that corrections of errors should in future only be made retrospectively by adjusting the amounts in the periods in which the errors occurred or by adjusting the opening balance of retained earnings of the first period presented. We endorse this procedure, which will enable financial statements to be compared in a meaningful way. We assume that the principle of materiality also applies to the correction of errors and suggest this aspect be explicitly included in the provisions of ED IAS 8.32.

Question 2:

Do you agree with eliminating the distinction between fundamental errors and other material errors (see paragraphs 32 and 33)?

Reply:

Yes, we agree with eliminating the distinction between fundamental errors and other material errors.

Additional remarks

Under ED IAS 8.19, entities which do not apply standards that have already been adopted by the IASB but have not yet come into effect will be obliged to disclose in the notes information such as the nature of the future change in accounting policy and an estimate of the effect of the change on the entity's financial situation.

Experience shows that it is not effective to disclose several assigned values and thus different results for the same period or the same item. Such an approach is extremely difficult to explain, since it inevitably raises the question as to the "correct" result. This does not necessarily make the financial statements more understandable or comparable. In our view, therefore, an obligation or, in many cases, a recommendation to disclose such information does not make good sense.

Furthermore, given the lack of time, it is often not possible to guarantee that the disclosed information will be meaningful. An entity is only really in a position to make sound statements about the effects of changes after full implementation of a new standard. A detailed explanation of the effects of a change before actually applying the new standard for the first time would be tantamount to a "trial" application and is to be firmly rejected. To take IAS 39 as an example: it would have been impossible to forecast the exact consequences without an analysis so detailed it would have been tantamount to an initial application.

IAS 21 The Effects of Changes in Foreign Exchange Rates

Question 1:

Do you agree with the proposed definition of functional currency as "the currency of the primary economic environment in which the entity operates" and the guidance proposed in paragraphs 7-12 on how to determine what is an entity's functional currency?

Reply:

Yes, we agree with the proposed definition of functional currency as the currency of the economic environment in which the entity primarily operates. This results in a clear distinction between the "functional currency" and the "presentation currency". We endorse the view that the functional currency is to be determined by applying the criteria in ED IAS 21.7 – 21.12, while there will be a free choice of presentation currency.

Question 2:
Do you agree that a reporting entity (whether a group or a stand-alone entity) should be permitted to present its financial statements in any currency (or currencies) that it chooses?

Reply:
Yes, we agree with the view that the presentation currency should not be tied to the functional currency. Normally, the presentation currency will probably be the same as the functional currency. Nevertheless, it is conceivable that there will be situations where choosing another presentation currency makes good sense, or is even indispensable. This arrangement will, for example, enable a subsidiary company to prepare its financial statements in the same currency as its parent, even if it has a different functional currency. Entities which choose to present their accounts in a currency other than the functional currency should indicate the reason in the notes, however. We would suggest making this a requirement.

Question 3:
Do you agree that all entities should translate their financial statements into the presentation currency (or currencies) using the same method as is required for translating a foreign operation for inclusion in the reporting entity's financial statements (see paragraphs 37 and 40)?

Reply:
Yes, we believe it is appropriate to have uniform rules for translating foreign-currency operations and items. The application of uniform translation methods makes financial statements more meaningful and enables relevant comparisons to be drawn between companies.

Question 4:
Do you agree that the allowed alternative to capitalise certain exchange differences in paragraph 21 of IAS 21 should be removed?

Yes, we agree with the elimination of the allowed alternative treatment.

Question 5:

Do you agree that

(a) goodwill and

(b) fair value adjustments to assets and liabilities

that arise on the acquisition of a foreign operation should be treated as assets and liabilities of the foreign operation and translated at the closing rate (see paragraph 45)?

Reply:

The wording of ED IAS 21.45 is not sufficiently clear, in our view. Irrespective of possible difficulties in interpretation, however, goodwill amortisation and write-downs on revalued assets should continue to be possible on the basis of historical rates. This is in line with the usual technique of calculating goodwill in already translated financial statements in the course of capital consolidation and carrying it over. We are therefore in favour of retaining the old rule.

Additional remarks

In our view, many of the rules in ED IAS 21 are hard to understand and will be difficult to implement in practice. For example, the scope of ED IAS 21.36 ff is not clear in relation to that of ED IAS 21.42 ff. In the interests of – at least partial – clarification, we suggest changing the subheading "Translation of a Foreign Operation" to "Consolidation Differences".

IAS 24 Related Party Disclosures

Question 1:

Do you agree that the Standard should not require disclosure of management compensation, expense allowances and similar items paid in the ordinary course of an entity's operations (see paragraph 2)?

"Management" and "compensation" would need to be defined, and measurement requirements for management compensation would need to be developed, if disclosure of these items were to be required. If commentators disagree with the Board's proposal, the Board would welcome suggestions on how to define "management" and "compensation".

Reply:

No, we do not agree with this approach. Information about management remuneration (including all elements such as bonuses and pension benefits) is highly important and relevant for investors – especially in light of the development of this form of compensation in recent years.

In Germany, for example, a requirement to disclose this information is set out in Section 285 no 9a of the German Commercial Code. The new German Transparency and Disclosure Act (*Transparenz- und Publizitätsgesetz*) also requires full disclosure of all forms of remuneration. In terms of the greatest possible transparency of financial statements, the IAS should not fall short of national rules in this area. The problems of definition and measurement which are mentioned are not adequate impediments in this respect.

In our view, the term "management" within the meaning of the standard covers the entire top management level of an entity. "Compensation" should cover all forms of remuneration.

Question 2:
Do you agree that the Standard should not require disclosure of related party transactions and outstanding balances in the separate financial statements of a parent or a wholly-owned subsidiary that are made available or published with consolidated financial statements for the group to which that entity belongs (see paragraph 3)? (Note that this proposal is the subject of alternative views of Board members, as set out in Appendix B.)

Reply:
No, we do not agree with this proposal. Related party information is essential to evaluating an individual entity's financial situation (on the basis of separate financial statements). The separate financial statements of an entity belonging to a group also have an important role to play – in calculating dividends, for example, particularly in continental Europe. Information on related parties is consequently also of interest to investors at the level of separate financial statements. Cases where the vast majority of an entity's transactions are internal provide a clear illustration that this information is indispensable.

The alternative disclosure of related party information in the consolidated financial statements does not have the same information value as in the separate financial statements – particularly if the group involved is large compared to the subsidiary entity. Under certain circumstances, the information might be omitted because of materiality considerations – on the basis of group level thresholds.

Additional remarks
We feel the level of detail required by ED IAS 24.14 is too high. In particular, the requirements in ED IAS 24.14 (b) and (c) cannot, in our view, be regarded as minimum disclosure. We suggest drafting a general disclosure requirement. It should, however, be up to the company to determine in what form the information is provided.

IAS 27 Consolidated and Separate Financial Statements

Question 1:
Do you agree that a parent need not prepare consolidated financial statements if all the criteria in paragraph 8 are met?

Reply:
The draft standard envisages restricting exemptions from preparing consolidated financial statements. In future, an exemption is only to apply with the agreement of all minority shareholders, if the entity's securities are not publicly traded and if there are no immediate plans for a public issue.

We reject a general obligation to prepare consolidated financial statements for subsidiary companies which issue only publicly traded debt securities or have plans to do so in the near future. In our view, there is a need for some differentiation in the rules, since the level of information and protection required by creditors cannot be equated with that required by shareholders. Creditors normally obtain the information they require from the consolidated financial statements of the parent company, not from sub-consolidated or separate financial statements. The additional costs that would arise in preparing such sub-consolidated financial statements would be out of all proportion to the additional benefit they could offer investors.

We would also like to point out that in many countries, the preparation of consolidated and/or separate accounts is regulated by capital market or stock exchange law, not in accounting standards.

Question 2:
Do you agree that minority interests should be presented in the consolidated balance sheet within equity, separately from the parents shareholders' equity (see paragraph 26)?

Reply:
We do not consider this change problematic. On the other hand, we see no valid justification for this U-turn by the IASB, so the change appears arbitrary. Given the ultimate objective of convergence between IAS and US GAAP, we would also like to point out that this rule runs counter to the US GAAP, which require minority interests to be presented as debt capital.

Question 3:

(a) *Do you agree that investments in subsidiaries, jointly controlled entities and associates that are consolidated, proportionately consolidated or accounted for under the equity method in the consolidated financial statements should be either carried at cost or accounted for in accordance with IAS 39, Financial Instruments: Recognition and Measurement, in the investor's separate financial statements (paragraph 29)?*

(b) *Do you agree that if investments in subsidiaries, jointly controlled entities and associates are accounted for in accordance with IAS 39 in the consolidated financial statements, then such investments should be accounted for in the same way in the investor's separate financial statements (paragraph 30)?*

Reply:

(a) There is no apparent reason why application of the equity method should no longer be permitted in the separate financial statements since this method, in particular, allows for a net asset value approach. We are in favour of retaining the existing three alternatives, i.e. accounting for these investments at cost, using the equity method, or as available for sale financial instruments in accordance with IAS 39.

(b) If non-consolidated entities are accounted for in the consolidated financial statements as available for sale financial instruments in accordance with IAS 39, ED IAS 27.30 makes the same treatment mandatory in the separate financial statements. This rule is tantamount to specifying that the accounting treatment applied to the separate financial statements will be dictated by that used in the consolidated financial statements. We firmly reject this approach and advocate a freedom of choice for the separate financial statements, irrespective of the treatment in the consolidated financial statements.

Additional remarks

The title of the standard does not in any way reflect its content or objectives. We suggest replacing it with "Presentation of Subsidiaries in the Separate and Consolidated Financial Statements of the Parent".

We foresee practical problems in applying ED IAS 27.12B. The listed criteria are insufficiently objective. If an entity holds just under half the voting rights in another entity, it would normally be just as easy and quick to acquire the shares needed to cross the 50% threshold on the market as it would to exercise options. In our view, the only sensible and practicable method of determining whether a controlling influence exists is to focus on present ownership interests. This would also bring the rule into line with ED IAS 27.15A, which states that potential voting rights are not to be taken into account in determining equity and minority interests.

We regard the twelve-month maximum period for the disposal of a subsidiary specified in ED IAS 27.13 as rather arbitrary. From an economic point of view, it makes little sense to set a specific period of time, since the convertibility into cash of equity holdings depends first and foremost on market conditions. We are therefore in favour of retaining the existing wording "in the near future".

The reason for the change in ED IAS 27.21 is not clear to us. We agree with the principle that consolidated financial statements should be prepared using uniform accounting and valuation methods. We also feel there is a self-evident need to take the principle of materiality into account and suggest reinstating the old wording.

The profit or loss from the disposal of a subsidiary is the difference between the proceeds from its disposal and the book value of the net assets. ED IAS 27.23 explicitly states that the cumulative amount of any exchange differences that relate to the subsidiary recognised in equity are to be recognised as income. It is not clear to us why only amounts from exchange differences are mentioned. In the interests of having a requirement which is less casuistic and more principle-based, we suggest a rewording stating that all amounts previously recognised in equity are now to be recognised as income.

The disclosure requirements in ED IAS 27.32 and 27.33 have been extensively modified, without there being any apparent reason for the changes. The requirement to list significant subsidiaries has been deleted, for example, in spite of the fact that this information is particularly valuable and of concrete use to users. On the other hand, new disclosure requirements have been included whose usefulness is not at all clear to us, e.g. ED IAS 27.32(e), 27.33(a) and 27.33(c). We advocate retaining the existing, tried and tested, disclosure requirements.

We also suggest integrating SIC 12 "Consolidation – Special Purpose Entities" into this standard.

IAS 28 Accounting for Investments in Associates

Question 1:
Do you agree that IAS 28 and IAS 31, Financial Reporting of Interests in Joint Ventures, should not apply to investments that otherwise would be associates or joint ventures held by venture capital organisations, mutual funds, unit trusts and similar entities if these investments are measured at fair value in accordance with IAS 39, Financial Instruments: Recognition and Measurement, when such measurement is well-established practice in those industries (see paragraph 1)?

Reply:
Yes, we agree with this rule. In the interests of legal certainty and equal treatment, we suggest including definitions of "venture capital organisations, mutual funds, unit trusts and similar entities".

Question 2:
Do you agree that the amount to be reduced to nil when an associate incurs losses should include not only investments in the equity of the associate but also other interests such as long-term receivables (paragraph 22)?

Reply:
The change brings this rule more into line with US GAAP (EITF No. 98-13). In principle, we agree with the proposal that, in the event of zero equity value, securities such as preference shares and near-equity receivables should also be included in the loss anticipation. However, this should only happen if the value of these securities can really no longer be guaranteed. A negative equity, or a negative equity value, is not necessarily an indication that all other receivables have also lost their value. In valuing collateralised receivables, for example, the value of the collateral must also be taken into account.

Additional remarks

Under ED IAS 28.5A, currently exercisable options and conversion rights must be included when assessing whether an entity's share of voting rights is likely to give it significant influence. We foresee practical problems in applying this paragraph. The listed criteria are insufficiently objective. If an entity holds just under 20% of the voting rights in another entity, the shares needed to cross the 20% threshold could be acquired just as quickly and easily on the market as by exercising options. In our view, the only sensible and practicable method of determining whether a significant influence exists is to focus on present ownership interests (see also our comments on IAS 27).

ED IAS 28.8 makes application of the equity method mandatory for associates. This is somewhat at odds with IAS 27, which explicitly excludes the equity method for separate financial statements. The rules on the correlation between separate and consolidated financial statements lack consistency and logic, in our estimation. We would ask for these rules to be revised with a view to establishing uniform standards for separate financial statements. In addition, it is not clear to us why changes in fair value when accounting in accordance with IAS 39 should be recognised in the profit and loss account.

We regard the twelve-month maximum period for the disposal of an associated company specified in ED IAS 28.8 as rather arbitrary. From an economic point of view, it makes little sense to set a specific period of time, since the convertibility into cash of an investment in an associate depends first and foremost on market conditions. We are therefore in favour of retaining the existing wording "in the near future" (see also our comments on IAS 27).

ED IAS 28.18 requires a difference of not more than three months between the reporting date of the associated company and that of the consolidated accounts. We do not believe this requirement would work in practice. The investor does not control the associated company, and thus has no possibility of influencing – let alone determining – its reporting date. We should like to make the general point that not all rules which make good sense when applied to fully consolidated entities can be successfully adapted to associated companies.

This is also true of the application of group accounting and valuation methods, for example: in practice, they cannot be applied to associated companies. The required information is not normally made available by the associates, so uniform accounting and evaluation methods cannot be guaranteed.

The disclosure requirements in ED IAS 28.27 have been considerably modified and extended. There is no obvious additional benefit for users, however. The requirement to list significant associates, including the share held of ownership interest and voting power, has been deleted. In contrast, ED IAS 28.27(a) – (g) lists a substantial number of new disclosure requirements, whose usefulness cannot justify the additional work they would involve. In our view, all essential information is to be found in the list of associated companies which had to be provided up to now. We recommend retaining the old rule (see also our comments on IAS 27).

IAS 33 Earnings Per Share

Question 1:

Do you agree that contracts that may be settled either in ordinary shares or in cash, at the issuer's option, should be included as potential ordinary shares in the calculation of diluted earnings per share based on a rebuttable presumption that the contracts will be settled in shares?

Reply:

We agree with this proposal. These potential ordinary shares should be included in the definition of the item "diluted earnings per share" because of the probability of actual dilution when calculating the item.

Question 2:

Do you agree with the following approach to the year-to-date calculation of diluted earnings per share (as illustrated in Appendix B, examples 7 and 12)?

(a) The number of potential ordinary shares is a year-to-date weighted average of the number of potential ordinary shares included in each interim diluted earnings per share calculation, rather than a year-to-date weighted average of the number of potential ordinary shares weighted for the period they were outstanding (i.e. without regard for the diluted earnings per share information reported during the interim periods).

(b) The number of potential ordinary shares is computed using the average market price during the interim periods reported upon, rather than using the average market price during the year-to-date period.

(c) Contingently issuable shares are weighted for the interim periods in which they were included in the computation of diluted earnings per share, rather than being included in the computation of diluted earnings per share (i.e. the conditions are

satisfied) from the beginning of the year-to-date reporting period (or from the date of the contingent share agreement, if later).

Reply:

(a) The calculation of the earnings per share on the basis of the year-to-date weighted average of the number of potential ordinary shares included in each interim diluted earnings per share calculation (compared to the year-to-date weighted average of the number of potential ordinary shares weighted for the period they were outstanding) is not clear in examples 7 and 12 and is very difficult to follow.

In our view, the **more appropriate calculation method** is to calculate the annual average on the basis of the period actually affected.

The approach based on a quarterly allocation results here in a distortion of this key figure.

(b) The described procedure can be endorsed if the average market price per quarter is identical to the year-to-date average. Should there be discrepancies, however, this method will also result in distortions.

(c) See reply to (b).

Additional remarks

As it stands, ED IAS 33 proposes extensive changes to the existing standard, focussing primarily on the definition and calculation of the denominator (number of shares) of "earnings per share" and "diluted earnings per share". In contrast, as indicated in the objective of the standard, the calculation of the underlying numerator "earnings" remains unresolved.

These changes – depending on the types of share and fluctuations involved – will require substantial additional work to be performed compared to existing methods. We see no additional benefit, however. The higher degree of accuracy which the changes are evidently intended to achieve do not, in our opinion, justify the additional time and effort involved.

Should you require any further information, please do not hesitate to contact us.

Yours sincerely,

Dr. Wolfgang Arnold Dr. Katrin Burkhardt