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The Technical Director
International Accounting Standards Board
30 Cannon Street
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UNITED KINGDOM

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Dear Sir

Exposure Draft of Proposed Improvements to International Accounting Standards

We are responding to the invitation to comment on the above exposure draft on behalf of the worldwide organisation and Global IAS Board of PricewaterhouseCoopers.

We welcome the Board's proposals in the exposure draft to make necessary improvements to some of the existing International Accounting Standards. However the 400 or so pages in this exposure draft are just the first step. The Board needs to accelerate its review of the standards not covered in this update, to enable those converting to IAS in 2005 or earlier to have as much certainty as possible, well before implementation.

Undue cost or effort

The Board has introduced the concept of "undue cost or effort" in the proposed changes to a number of the standards. We believe that this phrase is capable of interpretation in a lenient manner which may undermine the quality of financial reporting and comparability between periods and between companies. We recommend that the Board provides guidance that providing reliable and comparable information is a demanding standard which should be met, and that only in very rare cases would obtaining such information represent an undue cost to obtain the relevant information.

Introduction to each standard

The Board decided in April 2002 to amend the introduction paragraph to each standard to state that it should not apply to immaterial items and to delete any reference to paragraph 12 of the old preface. This has not been done in the exposure draft. In addition, the Board should address this point in respect of those Standards not covered by this Improvements project.

Proposed effective date

If the Board finalises the revised IASs in quarter 1 of 2003 (as implied by IASB Insight – July 2002) we believe that the proposed effective date for periods beginning on or after 1 January 2003 is too ambitious, particularly for entities with quarterly or half-year reporting under IAS 34. We recommend that the Board mandate an effective date for periods beginning on or after 1 July 2003, with early adoption encouraged.

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 paragraphs 13 - 16)?

No. We support strongly the retention of the true and fair override to be applied when the primary statements are misleading such that they do not give a true and fair view. However, we do not support the proposal in paragraph 15 not to adjust the primary statements in jurisdictions where an override is prohibited in the law. We believe that IAS should continue to set standards that are independent of national laws, as to do otherwise risks the intrusion of legal measures in this and other areas that may mean that IAS compliant financial statements will not be able to be comparable between jurisdictions.

As a matter of principle, we do not believe that recognition or measurement problems that result in misleading primary financial statements can be resolved by disclosure. Existing IAS 1.12 should be retained. If the Board continues with the approach in paragraph 15, we believe the Board must discuss this with the IAASB before finalising this revised standard, as we would expect to modify our audit report in such circumstances to conclude that the primary statements do not give a true and fair view.

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)?

Yes. However, the deletion of the definition of "extraordinary" in IAS 8 will mean that the revision will be unenforceable. The revised standard needs to make it clear what is being prohibited – calling an item extraordinary?, or separating an item on the face of the income statement, which is then not included in a total of like items? We believe it should be the latter.

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)?

Yes. This reflects the conditions that existed at the balance sheet date and is consistent with IAS 10.2(b). However, the wording in the first sentence of paragraph 61 appears to be inconsistent with paragraph 60. The former states that an obligation due to be repaid within 12 months of the balance sheet date can be shown as non-current on the basis of an expectation of refinancing. Paragraph 61 should be amended to clarify that if refinancing is at the sole discretion of the entity and not the lender, the liability should be classified as non-current if the entity has a contractual right to rollover or refinance for at least 12 months after the balance sheet date.

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 paragraph 62)?

Yes. This reflects the conditions that actually existed at the balance sheet date and is consistent with IAS 10.2(b).

(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 paragraphs 63 – 64)?

No. Paragraphs 62 and 63 contradict each other. Paragraph 62 indicates that if, at the balance sheet date, there is a breach of the covenant then the liability must be classified as current, even if the lender agrees not to demand repayment after the balance sheet date. Paragraph 63, on the other hand, indicates that if there has been a breach at the balance sheet date then the debt can be treated as non-current if the lender has agreed a grace period and the breach is either rectified after year-end and before the approval date or seems "likely" to be rectified.

The Board should adopt a consistent approach. It should select one principle: either post balance sheet changes to loan terms should result in reclassification, or they should not (the latter is as proposed in (a) above). Classification in the circumstances set out in (b) above should depend upon the period of grace that actually existed at the balance sheet date. Thus, if the period of grace agreed by the balance sheet date is less than 12 months a loan should be classified as current, but if the period of grace is more than 12 months a loan should be classified as non-current.

If paragraph 63 is retained in its current form, we believe that this requirement will be made more practicable for entities to apply, if item (b) in paragraph 63 is deleted and item (a) in paragraph 63 is clarified by starting with the words "after the balance sheet date and before the financial statements are authorised for issue".

Question 5

Do you agree that an entity should disclose the judgments 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)?

No. The current proposal is unclear and the example in paragraph 109 is unhelpful since use of the held-to-maturity category is rare in practice. We support disclosure of the judgments that led to <u>selecting</u> a particular policy where a choice is available under a standard. However, we do not support disclosure of the judgments made in applying policies, as we believe that this will lead to boilerplate text.

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 paragraphs 110-115)?

Yes. We agree that there should be greater disclosure of forward-looking information about the risks that are faced that could have a material effect on assets or liabilities within the next 12 months. However, we have significant reservations about the scope of this requirement and cannot see how it will be practical to ensure that all relevant risks are disclosed. The disclosures should be relevant and highlight the significant risks, rather than normal business risks that are common to similar entities. More guidance will be needed to implement this requirement in practice.

For example, what level of information needs to be given about the potential change in the demand for a product that might arise in the following year, and thus cause an impairment of plant and equipment? Does the disclosure have to anticipate extremes, such as abnormal changes in the weather or severe recession that could affect demand?

To be effective, and to avoid extensive boilerplate disclosures, the revised text must provide reasonable limits to circumscribe the assumptions and risks that must be addressed. In particular, the text should indicate that only those risks that may be expected to arise in the ordinary course of business and are reasonably foreseeable, need to be disclosed.

The Board should approach the SEC and other regulators before proceeding with these requirements as regulatory difficulties have been experienced in the past with including certain types of forward looking information in audited accounts published in the US capital markets.

Other comments on IAS 1

Paragraph 2. We support the observation in the second sentence that general purpose financial statements include those presented in a prospectus. However, the penultimate sentence of paragraph 6 of the Framework suggests that prospectuses are outside the scope of the Framework. We suggest that a consequential amendment is made to the Framework to conform the wording to proposed IAS 1.2.

Paragraph 54(c). The Board needs to adopt a consistent approach to PP&E held for disposal. According to existing IAS 1.57(b), an asset that “is held primarily for trading purposes or for the short-term and expected to be realised within twelve months of the balance sheet date” should be classified as a current asset. Hence, under existing IAS 1, PP&E held for disposal at the balance sheet date should be classified as a non-current asset.

However, under the proposed IAS 1.54(c) "when an asset is expected to be realised within twelve months of the balance sheet date", PP&E held for disposal would be classified as a current asset.Users of accounts may be confused by this treatment as PP&E are acquired and held primarily for long-term purposes. Furthermore, the Board's proposal in revised IAS 16.59 is that depreciation should continue to be provided on PP&E held for disposal. Accordingly we consider that PP&E held for disposal should continue to be classified as "non-current assets".

Paragraph 65(n). Proposed presentation of minority interest as equity. We agree that certain classes of minority interest are not liabilities in accordance with the definitions in the Framework. However, the Board's balance sheet classification is inconsistent with the presentation of minority interest as a line item before net profit (paragraph 76(h)). In addition, we believe that the positioning of minority interests within equity prejudges the outcome of the debate about the treatment of gains and losses on part disposals of subsidiaries, where we believe that all gains or losses relating to the parent shareholders should be recognised in the income statement.

Paragraph 75(b) of existing IAS. Proposed deletion of results of operating activities. We do not support the deletion of this line item. Its removal will result in significant confusion amongst preparers, users and auditors in the period until the Board publishes its new standard on reporting financial performance.

The proposal is inconsistent with paragraph 7 of the Invitation to Comment, which notes the Board's intention to exclude from the revision those issues in IAS 1 that may be addressed in its Reporting Financial Performance project. This proposal seems to prejudge the outcome of that debate.

We also do not support removal of the Appendix examples and paragraphs 80 and 82, as these help in clarifying the expenditures that should be charged in arriving at operating profit. The Board's approach will also cause difficulties with the application of other standards such as IAS 7 and IAS 14 that contain references to this line item, for which no compensating adjustments have been suggested in the Improvements Exposure Draft.

Paragraph 76. Proposed additional line item: Expenses. We strongly recommend the inclusion of an additional line item between revenue and finance costs titled: "Expenses". We believe that this would make a major contribution to improving comparability of operating results between companies that report under IAS.

Paragraph 82(a), (b), (e) and (g) . These appear redundant, as the disclosures are already required by other standards.

Paragraph 105(j). Delete "and investments" since these are examples of financial instruments.

Paragraph 116(b). This disclosure about cumulative preference dividends not recognised belongs more appropriately in the Board's proposed amendments to IAS 32. It should be deleted from IAS 1.

Paragraph 117(a). Legally, "domicile" means "the place where for official purposes one is considered to live". However, an entity might interpret this term as the entity's country or place of incorporation, while some might interpret this term as the entity's principal place of business. We suggest clarifying that this is the country of incorporation.

IAS 2, Inventories

Question 1

Do you agree with eliminating the allowed alternative of using the last-in, first-out (LIFO) method for determining the cost of inventories under paragraphs 23 and 24 of IAS 2?

Yes.

Question 2

IAS 2 requires reversal of write-downs of inventories when the circumstances that previously caused inventories to be written down below cost no longer exist (paragraph 30). IAS 2 also requires the amount of any reversal of any write-down of inventories to be recognised in profit or loss (paragraph 31).

Do you agree with retaining those requirements?

Yes. Reversals should be made when these provisions are no longer necessary.

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)

We support the requirement that all voluntary changes in accounting policy should be made retrospectively.

We agree that the use of the "fundamental error" approach can lead to important distortions in the trend of the results reported by companies and thus needs to be revised. Whilst we agree that material errors in the period(s) covered by the comparatives should be adjusted, we do not believe this should be extended further to such a degree that comparative amounts will be changed most periods for very small items. Thus accumulated errors that are not material to comparative periods, should be adjusted in the current year income statement.

Question 2

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

Yes. However, we are concerned that there may be difficulties in deciding whether reliable information was in existence at the time when the prior period financial statements were prepared, and suggest that this criterion be amended.

For example, assume a perpetrator of a fraud destroyed evidence such that reliable evidence was not available. The text should clarify that the accounts should be corrected using the best information now available, and not remain unadjusted on the basis that reliable evidence was not available at the time.

We are concerned about the application of paragraph 33 to an "error" situation. In such cases restatement of comparatives is necessary to ensure fair presentation and we believe it would be only in extremely rare cases that an entity, having already identified the existence of the error, could represent an undue cost or effort to obtain the relevant information.

Other comments on IAS 8

Paragraph 19. We are uncomfortable with the use of the "undue cost or effort" exemption in paragraph 19(d)(ii). The text needs to recognise that for many entities it is often impracticable to calculate the estimate of the financial impact until the entity has been able to analyse the new standard in depth.

IAS 10, Events After the Balance Sheet Date

No questions asked.

Other comments on IAS 10

Inconsistency between IAS 10, IAS 32 and IAS 37

The amendment to this standard and to IAS 37 does not remove the confusion over when to provide for a dividend.

We are not convinced that to declare a dividend (IAS 10) is the same as waiting until the dividend has been approved at an annual general meeting (IAS 37) or the same as having discretion over the payment of a dividend (IAS 32).

The Board needs to decide and make clear in IAS 10 whether the constructive obligation model should be applied in these circumstances. We believe that dividends should be provided when management no longer has the discretion to reduce the amount or to defer the payment indefinitely, consistent with the model in IAS 32.22 for preference dividends. IAS 10 paragraphs 11-12 and IAS 37 Example 12 should both be conformed with this principle.

IAS 15, Information Reflecting the Effects of Changing Prices

We support the withdrawal of this Standard. However, there is now a need to incorporate into IAS 29 some of the background to inflation accounting contained in IAS 15.

IAS 16, Property, Plant and Equipment

Question 1

Do you agree that all exchanges of items of property, plant and equipment should be measured at fair value, except when the fair value of neither of the assets exchanged can be determined reliably (see paragraphs 21 and 21A)?

Yes. Other than the exceptions discussed below, we agree with the principle that exchanges of property, plant and equipment should be measured at fair value, including exchanges of similar assets, except when fair value cannot be reliably determined.

It should also be made clear that the resulting gain (if any) should not be included in revenue. The Board should clarify that exchanges of fixed assets are excluded from the scope of IAS 18 and guidance should be added to IAS 16 paragraph 56 as to where they should be reported in the income statement.

Different principles are needed for such transactions between common controlled entities, and those principles should be consistent with those applied for business combinations between common controlled entities that the Board needs to address.

Question 2

Do you agree that all exchanges of intangible assets should be measured at fair value, except when the fair value of neither of the assets exchanged can be determined reliably? (See the amendments in paragraphs 34-34B of IAS 38, *Intangible Assets*, proposed as a consequence of the proposal described in Question 1.)

(Note that the Board has decided not to amend, at this time, the prohibition in IAS 18, *Revenue*, on recognising revenue from exchanges or swaps of goods or services of a similar nature and value. The Board will review that policy later in the context of a future project on the Recognition of Revenue.)?

Yes. Subject to the same reservations identified in question 1 above, we agree that the same principles should be applied to intangible assets. The guidance should be included to clarify that the fair value of the intangible asset given up should exclude any value for associated internally generated goodwill. The same proviso should exist as for PPE that gains on such items should not be reported in revenue.

Question 3

Do you agree that depreciation of an item of property, plant and equipment should not cease when it becomes temporarily idle or is retired from active use and held for disposal (see paragraph 59)?

No. We believe that there should not be a charge for depreciation when plant is retired from active use and held for disposal. Those assets carried at depreciated historical cost should be subject to an impairment test as a separable asset at that point and written down to their net selling price.

Plant that is temporarily idle should continue to be depreciated if the basis of depreciation is a simple time allocation. No depreciation should be provided if a unit of production basis is used (provided the total service potential of the plant is not reduced while lying idle).

Other significant comments on IAS 16

Residual values

We disagree with the proposal to amend the definition of residual values in paragraph 6 and 46 to reflect prices current at the balance sheet date, for assets held at historical cost, on the basis that this does not result in an accurate measure of depreciation, which is a measure of the wearing out of the asset. We believe that the resulting annual depreciation charge will become very difficult to understand – indeed it appears that it could become a credit in some contexts.

Whilst we understand the conceptual merit of not reducing the carrying amount of an asset below its value to the business, a move to an economic depreciation model would require other changes, such as to depreciation methods. Any change in approach should not be made on a piecemeal basis. We believe that the proposal is not consistent with the definition of depreciation in the standard, as it does not result in the 'systematic allocation' of the depreciable amount of an asset over its useful life. Neither does such a basis reflect the pattern in which the asset's future economic benefits are "expected to be consumed" by the entity as required by paragraph 41.

If the Board decides to retain its current proposal it should develop a set of 'triggers' similar to the approach in IAS 36 to determine when the reassessment of residual value should take place.

Cost capitalisation

We believe that the Board should have proposed consistent principles for the capitalization of costs in IAS 2, IAS 16 and IAS 38. This would be a major simplification.

Whilst the definitions and guidance in IAS 16.14-18 are similar to that in IAS 2, and paragraph 18 implies that the same costs would be capitalized, the guidance is inconsistent. This is particularly so in relation to the treatment of administration and other general overhead costs, which would not be capitalized under revised IAS 16.17, but would be capitalized under IAS 2.10-14.

We believe that IAS 16 should be made consistent with IAS 2, whilst clarifying that those items in paragraphs 17(a)-(c) and 17A should be excluded from the cost of property, plant and equipment. This would involve reinstating the first paragraph of paragraph 17 of IAS 16.

Other comments on IAS 16

Paragraph 7(b). We disagree with adding in paragraph 7(b) the wording about assets carried at fair value. The subsequent measurement basis addresses the use of fair values.

Paragraph 20A. The second sentence could be read as allowing the capitalization of dismantling, removal and restoration costs that arise due to operating activities during the asset's life. IAS 16 should clarify that such capitalization is permitted only if it meets the requirements for the capitalization of subsequent expenditure and that costs of restoring the site that arise from operating the asset, rather than from constructing, acquiring or enhancing the site, should be expensed as part of operating costs.

Paragraphs 22A-22D. These should clarify that separate components should be depreciated over their individual useful lives, as though they were separate assets, in accordance with paragraphs 41-48, rather than over the life of the overall asset. This section (together with paragraph 12) should also state that only material components should be treated as separate assets in this way. This should be linked to paragraph 26 where expenditure on immaterial replacements or renewals of property, plant and equipment may be treated as repairs and expensed when incurred.

Paragraphs 34-36. These should acknowledge that in extremely rare circumstances a reliable valuation of an asset within a class of assets may not be practicable. In such circumstances, IAS 16 should permit the revaluation of the remainder of the class of the assets and exempt that asset from being revalued. Additional disclosures should be made to explain which asset has not been revalued, its carrying amount, and the reasons why a valuation was not practicable.

Paragraph 37. This should require an adjustment for depreciation of revaluation gains recognised in income that reverse revaluation losses previously taken to income.

Paragraphs 38. This should require that any decrease be debited directly against any credit balance existing in the revaluation surplus in respect of that asset until the carrying value of the asset reaches its depreciated historical cost and, thereafter, it shall be recognised as an expense.

Paragraph 39. The transfer of additional depreciation charged on the revaluation gain to retained earnings as the asset is used should be made mandatory.

Paragraph 41. It is not clear from paragraph 41 at which point of time an entity should commence charging depreciation. In a normal situation, an entity will commence the operational use or trial test of an item of PP&E when the PP&E is “capable of operating in the manner intended by management” (according to proposed IAS 16.15(b)). However, some entities may argue that the Standard is not clear on this perspective and may delay depreciation even when the PP&E are ready or available for use but not yet put into operational use. This situation may occur in certain countries adopting a planned economy system under which the entity may not have full control of when to put an asset into operational use.

We recommend adding to paragraph 41 of IAS 16 the wording similar to IAS 38.79 “amortisation should commence when the asset is available for use”.

Paragraph 64(f). Where an asset is carried at a revalued amount, we do not agree with the requirement to disclose the amount at which the asset would be carried, if the historical cost basis had been used. If an entity has decided that fair value is relevant to users, presumably it thinks cost is less relevant. The benefits of this disclosure do not justify the costs involved.

Paragraph 66. The encouraged, but not required, disclosures should be deleted. Giving such additional information should be left to the discretion of the entity, depending upon the relevance of the item to the particular circumstances.

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IAS 17, Leases

Question 1

Do you agree that when classifying a lease of land and buildings, the lease shall be split into two elements – a lease of land and a lease of buildings? The land element is generally classified as an operating lease under paragraph 11 of IAS 17, *Leases* and the buildings element is classified as an operating or finance lease by applying the conditions in paragraphs 3-10 of IAS 17.

Yes, where this would result in classifying the building as held under finance lease and the land as held under an operating lease. However, we cannot see the merits of splitting land and building if both would be finance leases or both operating leases of a similar duration.

There are significant practical problems in arriving at the relative fair values of the two components. Our conversations with professional valuers have shown that they often do not believe that a reliable split can be made between land and buildings, particularly for an existing property. We agree that, where the lease cannot be split into its elements and the combined package is not clearly an operating lease, it should be presumed to be a finance lease as set out in IAS 17.11B. That paragraph should go on to emphasise that in such cases the entire leasehold land and buildings is treated as property, plant and equipment or as investment property (as appropriate).

However, this area would be greatly simplified by removing the requirement in IAS 17.11 that a lease of land can only be a finance lease if title can be transferred. Paragraph 11 contradicts paragraph 8 which requires that the classification depend on the transaction's substance. Whilst we agree that leases of land by themselves are often operating leases, we have experience of very long (e.g. 999 year) leases of land where the residual value at the end of the lease period is negligible, the annual rent is trifling and all of the value is in the capital leasehold interest. These are in substance finance leases, but for IAS 17.11. Entities should follow the guidance in IAS 17.8 and 9 to determine the classification for all property (whether investment property or PP&E) and this would ensure greater consistency with the amendment to IAS 40.

With the amendment to IAS 40, the Board has found a practical solution to a difficult issue. Nevertheless the Board needs to revisit IAS 17 as a separate, discrete project and in particular the conceptual basis for lease accounting as a matter of priority, to ensure a consistent conceptual approach in the treatment of leases of property, plant and equipment and of investment properties.

Question 2

Do you agree that when a lessor incurs initial direct costs in negotiating a lease, those costs should be capitalised and allocated over the lease term? Do you agree that only incremental costs that are directly attributable to the lease transaction should be capitalised in this way

and that they should include those internal costs that are incremental and directly attributable?

Yes, we support capitalization as this consistent with the model for financial instruments. However, the text should make clear that the capitalized costs should only be those that are directly attributable to the individual lease and should not incorporate the allocation of general overheads, such as those incurred by a sales and marketing team.

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?

Yes, we support the proposed definition of functional currency.

However, we have fundamental problems with the guidance for the determination of the functional currency. The key determinant should be the principal underlying currency that gives rise to volatility in operating gains and losses, i.e. those that give rise to the gross revenues and the costs of those sales. If finance is obtained from investors from a particular country or region, then entities should be able to select that currency as its presentation currency but we do not believe that this is particularly relevant to the selection of the overall functional currency.

The text of paragraphs 7(a), 7 (b) and 11 is confused. It needs to be rewritten to make clear that the underlying economics are more important than the currency in which transactions are denominated. We suggest the following text in place of paragraph 7 (a):

"the currency of the country whose competitive forces and regulations mainly influences sales prices, which may be the currency of settlement of sales transactions"

and similarly 7(b) should be rewritten as:

"the currency of the country whose competitive forces and regulations mainly influences labour, materials and other costs of providing goods or services, which may be the currency of settlement of such transactions".

Accordingly we believe that the example at paragraph 34 should be removed or amended to identify that a change in the underlying economic environment (not the denomination of transactions) might lead to a change in functional currency.

We also believe that additional guidance on the effects of national currency regulations should be given greater significance and examples given on matters such as special tariffs and currency restrictions.

It is not clear whether paragraph 8 should be regarded as subsidiary to paragraph 7 or whether both paragraphs should be given equal emphasis. Paragraph 8(b) should be incorporated into paragraph 7 and used to determine the appropriate functional currency.

The group as a single entity. In relation to a group, the principle that a group should be treated as if it were a single economic entity by itself demands that it should be required to determine its own functional currency by applying the same principles and guidance as required for individual entities. This is particularly important where investment holding companies are established in hard currency locations and invest principally in locations with soft currencies. The consequence of failing to require the determination of a functional currency of the group (which could be different from the functional currency of the parent as a separate entity) is that significant translation losses are lost in equity.

Paragraph 9 – determining a functional currency of a foreign operation. It is not entirely clear from the text of the standard whether the factors described in (a) through (d) should only be considered on a parent company (reporting entity) level, or should they be considered by foreign operations themselves, in their standalone (or sub-consolidation) accounts.

Consider the following example. Country A, that reports under local GAAP, has an off-shore subsidiary in Country B. The offshore subsidiary reports under IAS and needs to prepare standalone IAS financial statements. This subsidiary acts as the treasury center for the financing of the parent entity's operations in Continent C. The question is: should the offshore subsidiary in Country B consider factors listed in paragraph 9 when determining its own functional currency?

Paragraph 6 defines foreign operation as an entity that is a *"subsidiary…of a reporting entity, the activities of which are based or conducted in a country or currency other than those of the reporting entity"*. However, parent entity is not reporting under IAS and therefore would not necessarily be considered a reporting entity under IAS. On the other hand, paragraph 15 says that *"in preparing financial statements, the functional currency of each individual entity – whether a stand-alone entity, an entity with foreign operations (such as parent) or a foreign operation (such as subsidiary or branch) – is determined in accordance with paragraphs 6-12"*. This would suggest that the offshore subsidiary in Country B should determine its functional currency independently of the parent.

We believe that the intention is to require the offshore subsidiary to follow the guidance under paragraph 9 but would recommend the Board to clarify this issue.

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?

No. We do not believe that the selection of presentation currency should be a free choice. Reporting entities should be restricted to present statements in their functional currency or in a currency relevant to shareholders. We believe that paragraph 8(a) should be applied in addition to paragraph 7 when selecting the presentation currency, but it should not be taken into account when determining the functional currency.

Further we believe that the text of paragraph 8 also needs revision to identify that the needs of the primary providers of capital may be the most relevant criteria governing the selection of a presentation currency.

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)?

No. The method of translation should preserve the relationships that are present in the functional currency, otherwise this will distort the relative growth in sales, profit and other key measures. Accordingly, we support the use of the closing rate method for the reasons set out in paragraph A14 to the proposed Appendix to revised IAS 21.

Question 4

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

Yes. However, the Board should at the same time prohibit capitalization of exchange differences under paragraph 5(e) of IAS 23 to avoid arbitraging between the two standards.

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)?

Yes.

Other comments on IAS 21

Paragraph 24. Further guidance would be helpful on what to do where there is a temporary suspension of an exchange rate. We believe that the best effort should be made to determine what rate would have been present had exchanges in fact been open on the relevant day, and in the absence of other evidence we would use the opening rate of the first trading day thereafter.

Paragraph 52. Changes should only be made when the new basis is more relevant that the previous basis or there has been a change in facts and circumstances. Thus disclosure should be required of the reason for any change in functional or presentation currency.

Paragraph 37. This paragraph differs from the old paragraph 30 of IAS 21 as it relates to the translation of equity items. Paragraph 37 now states equity items should be translated at the closing rate. Old paragraph 30 "implied" that equity items be translated at historical rate. By using the closing rate for equity items, the CTA will no longer include an exchange difference between translating opening net assets at historical rate and translating net assets at closing rate. This is inconsistent with paragraph 39(b) which states that exchange differences result from translating opening net assets of a foreign entity at an exchange rate different from that at which they were previously reported.

We believe that paragraph 37 introduces a significant change from the existing paragraph 30. We do not believe that this change is warranted, as we are not aware of any significant practice issues with the current translation model.

Currency risk disclosures. We will be commenting upon the proposed revisions to IAS 32 in due course. However, we note that the Board has not addressed the lack of guidance on making disclosures about spot and forward currency positions in either the revision to IAS 32 or IAS 21.

PRICEWATERHOUSECOOPERS

The Technical Director
9 September 2002

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'.

No. The compensation and other transactions and balances with key management of a group is a matter that is relevant to decisions taken by users of financial statements and regularly results in high-profile comments by analysts and the press. Thus we believe that IAS 24 should be amended to make it clear that all material transactions with key management should be reported and that materiality should be judged by reference to the related parties. We do not believe that there is any need to report separately the remuneration of other management.

The definition of key management is contained in IAS 24. We believe that it does not need adjustment for this purpose.

A definition of "compensation" is unnecessary. The existing requirement is to disclose all material related party transactions. Thus it would include all capital and revenue transactions and balances, and not just compensation. Compensation should be shown separately from other items, eg capital and revenue transactions with directors. We believe that transactions and balances with key management should be aggregated.

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).

No. We believe that generally there is little difficulty in subsidiaries identifying related party transactions.

If the Board follows the proposed approach, the separate financial statements should require a note disclosure referring readers to the relevant disclosures in the consolidated financial statements of the parent entity. In the absence of such a comment the readers may assume there are no transactions with these related parties. We do not believe it is appropriate to assume readers would know of the existence of these transactions or which financial statements they should refer to to find the disclosures.

Other comments on IAS 24

We support the removal of the exemption for state-controlled enterprises from disclosing transactions with other state-controlled enterprises. However, we believe it may be appropriate in certain circumstances to permit a higher level of aggregation than contemplated by the current standard. For example, in a state controlled economy it may be the case that substantially all of certain line items comprising transactions or balances are with state controlled entities. For example, it will be impossible for a state-controlled entity that operates retail gas stations to accumulate and summarise retail gasoline sold to other state-controlled entities. It will also be very difficult for the entity to keep track of purchases from other state-controlled entities. In such a case , a statement of the general extent of such transactions should be sufficient because it will often be impractical for these entities to identify all the related parties they are dealing with and to make the detailed disclosures required by the standard.

Paragraph 3. This paragraph should clarify that the consolidated financial statements should be prepared in accordance with IAS.

Paragraph 4. The existing paragraph 4(a) explicitly states that intra-group related party transactions need not be disclosed in consolidated financial statements. It is not clear whether we can construe that the proposed paragraph 4, which states that intra-group related party transactions and outstanding balances are eliminated in the consolidated financial statements, has the same meaning as the existing paragraph 4(a). We suggest adding at the end of paragraph 4 the following words “and are therefore not disclosed in the consolidated financial statements”.

Paragraph 9. The definition of “close members of the family of an individual” has not explicitly included siblings (brothers and sisters) and parents of an individual. We recommend adding this to the definition for clarity.

Paragraph 9. Section (f) provides clear guidance when the relationship of control or significant influence exists via an individual or key management. But the wording is not clear whether two entities that are subject to common significant influence / common joint control of another entity (as opposed to an individual) are considered as related parties. The same logic should apply where the relationship of significant influence exists via an entity. This could be accomplished by extending paragraph 9(a) to specify that the reporting entity is related to associated undertakings and joint ventures in the group of which the reporting entity is a subsidiary.

Paragraph 12. We strongly encourage the IASB to expand the disclosure requirements in IAS 24.12 to include requirements to disclose the name of the ultimate controlling party. We believe strongly that disclosure of the name of the ultimate controlling party is relevant and useful information for users of financial statements and should be required. Without this disclosure, it is very difficult for users of the financial statements to fully understand the nature of the control that is exercised over the reporting entity.

Paragraph 14. We also strongly encourage the IASB to expand the disclosure requirements to include requirements to disclose the name of the transacting parties. We believe that the requirement to disclose the name of the related party is essential for a full and complete understanding of the nature of the related party relationship and the transaction being disclosed. Without the name of the related party involved, it is not possible for users of financial statements to consider the full range of potential effects of transactions with that related party. This will limit the assessment that users of financial statements can make of the effectiveness of an entity's operations which is one of the key reasons for requiring related party disclosures. It will be necessary to recognise that this must not result in a breach of a legal duty of confidentiality, so disclosure that the law has prohibited disclosure of the name would be necessary in such circumstances.

The minimum disclosure requirements per paragraph 14 should be amended to specifically include as a subparagraph "information about the transactions and outstanding balances necessary for an understanding of the potential effect of the relationship on the financial statements". It would be helpful if this general requirement were included in the list of minimum disclosures. There is a possibility that paragraph 14 may be interpreted such that if the listed minimum disclosures a)-d) are made that this meets the requirements of the paragraph. We believe that as a minimum, disclosures should include not only items a)-d) but also any other information necessary for an understanding of the related party transaction.

PRICEWATERHOUSECOOPERS

The Technical Director
9 September 2002

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?

Yes. However, the text needs to clarify that the dispensation should be available when any parent publishes IAS compliant consolidated financial statements. It should not be restricted to just the immediate parent or the ultimate parent. Paragraph 33(b) should also be amended to align with these proposals.

Paragraph 8(c) could be easier to interpret if the exemption was prohibited when the parent was contemplating within the next 12 months the issue of securities in public securities markets.

Question 2

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

Yes. We accept that they meet the definition of equity in the Framework.

The IASB has indicated that the recognition and measurement of minority interests will be considered in Phase II of the Business Combinations project. We believe that any changes in the presentation of minority interests should be deferred until the recognition and measurement issues are resolved and a proper debate on the merits has taken place.

Question 3

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)?

Yes.

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)?

Yes.

Other comments on IAS 27

Paragraphs 4 and 6. The definition of separate financial statements is given in paragraph 4,whilst the key definitions used in the draft standard are given in paragraph 6. The definition of separate financial statements should be given together with the other key definitions in paragraph 6. The second sentence of the definition of separate financial statements would be clearer as follows: "Separate financial statements are also financial statements prepared by a parent that meets the conditions in paragraph 8 and does not prepare consolidated financial statements."

Paragraph 8 and 9. We believe that a parent meeting the conditions in paragraph 8 should be able to prepare consolidated or separate financial statements or both, and that the drafting of these paragraphs should make this clear. Paragraph 9 seems to imply that only stand alone financial statements could be prepared. These paragraphs need to be rewritten to make clear that they do not prohibit a subsidiary from preparing group accounts.

Paragraph 12A. This paragraph should be strengthened to make clear that these restrictions have to be so significant as to prohibit access to economic benefits.

Paragraph 12B This paragraph incorporates the conclusions of SIC-33. Whilst we agree that potential voting rights provide the final evidence of control in some cases, the existence of potential voting rights does not always result in the power to govern the financial and operating policies of the underlying entity. We believe the inclusion of elements of SIC-33 has the effect of unbalancing the text of this standard and out of preference we would have left SIC-33 as an interpretation. If it is to be retained, then balance should be retained by increasing the emphasis that all the facts and circumstances of each case should be examined in reaching a conclusion based on the underlying substance.
If SIC-33 is incorporated into IAS 27, the Appendices to SIC-33 should also be included as Appendices to IAS 27.

Paragraph 13. This should be amended to provide that a subsidiary that has not been sold within 12 months then must be subsequently consolidated. However, if a binding sale agreement is in place by the date of preparation of the subsequent annual financial statements, we believe that there is little benefit to be gained from consolidating in the second accounting period post acquisition, only to deconsolidate shortly thereafter. In such circumstances the entity should disclose why consolidation has not subsequently taken place and give details of the transaction.

Paragraph 15A. This paragraph requires the allocation to minority interests based on current ownership interests. We do not agree that this will always be appropriate and believe that this conflicts with the requirement to record deferred consideration on an acquisition. For example, the substance of the potential interests in shares acquired by way of a forward purchase or a deep in the money call option may be deferred consideration that should be recorded at the outset in accordance with IAS 22.23.

Paragraph 15A has not considered the situation when the share of an investee's profit between the major and minority shareholders is not determined based on ownership interests but each party's rights and obligations under separately agreed terms. For instance, investors may share the profit based on an agreed ratio set out in the shareholder agreement. We suggest rewording paragraph 15A to clarify this situation.

Paragraphs 17 and 18. These paragraphs could usefully be expanded to specify the extent to which the elimination of intra-group transactions should be allocated to minority interests.

Paragraphs 19 and 20. We believe these should be expanded to specify that prior period comparatives should be restated to opening retained earnings when a subsidiary changes its reporting date to be consistent with the parent so that periods of consistent length are reported, and no period receives the benefit of a one off "catch up."

Paragraph 23. This deals with the accounting implications of the disposal of a subsidiary, but does not address a partial disposal or a deemed disposal, where it remains a subsidiary or becomes an associate. We believe it should confirm that similar principles are applied as are set out in SIC 13 and that gains (if any) should be recognised on all such transactions and that such events should be treated as impairment triggers.

Paragraph 29. We believe this paragraph should be amended so it refers also to parent entities that do not prepare consolidated financial statements, as a parent that meets the conditions in paragraph 8 would not necessarily prepare consolidated financial statements.

Paragraph 29A. This should be amended to delete the words "that purport."

Paragraph 29B. This repeats the definition of the cost method given in paragraph 6 and should be deleted, with the final sentence of this paragraph incorporated in paragraph 6.

Paragraph 30. We believe this paragraph should be amended so it refers also to parent entities that do not prepare consolidated financial statements.

Paragraph 32 (a) (old). We believe the listing of principal subsidiaries (probably no more than 5-10), together with information about ownership and location, can be useful to users of financial statements, in particular where there are minority interests. We believe this disclosure requirement should be retained.

Paragraph 32 (b) (new). We do not believe there is any benefit from including summarised financial information on non-consolidated subsidiaries if there is a binding sale agreement in place before the date of completion of the financial statements. In such circumstances details of the terms of the disposal should be given.

Paragraph 32 (b) (iv) (old). We do not believe the requirement to disclose the effects of the acquisition and disposal of subsidiaries should be deleted. This information is helpful to users of the financial statements and it should be retained, indeed we would have suggested that it should be enhanced.

Paragraph 33. These disclosures are unnecessary.

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)?

Yes. However, we feel that the text needs to be clear that this approach may also be used by any entity (eg banks and insurance companies) which holds such assets for their marketable value. The Standard should also emphasise that an entity which holds these assets as a medium through which it carries out its own business, should apply equity accounting.

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)?

Yes. We believe that accounting for losses should cease when all such interests have been taken into account. However, such interests should first be tested for individual impairment in accordance with IAS 39 until such time as they are reduced to nil as a result of equity accounting the losses.

Other comments on IAS 28

Paragraph 5A This paragraph incorporates the conclusions of SIC-33. Whilst we agree that potential voting rights provide the final evidence of significant influence in some cases, the existence of potential voting rights does not always result in the ability to significantly influence the financial and operating policies of the underlying entity. We believe the inclusion of elements of SIC-33 has the effect of unbalancing the text of this standard and out of preference would have left SIC-33 as an interpretation. If it is to be retained, then balance should be retained by increasing the emphasis that all the facts and circumstances of each case should be examined in reaching a conclusion.

Paragraph 5A. This explains how the group's interest in an associate is calculated. We do not agree that it will always be appropriate to treat derivatives as other than present interests. We believe that this conflicts with the requirement to record deferred consideration on an acquisition. For example, the substance of the potential interests in shares acquired by way of a forward purchase or a deep in the money call option may be deferred consideration that should be recorded at the outset in accordance with IAS 22.23 – IAS 28.16 says that similar principles should be applied as are applied to subsidiaries.

Paragraph 6. This states that the investor's share of direct equity movements recorded by an associate are recognised in equity by the investor. The guidance could usefully also deal with some of the detailed issues that will arise in practice, such as the treatment of equity movements when the investor's interest in the associate changes or the interaction between such equity movements and the guidance dealing with losses.

Paragraph 8A. This paragraph could be read to say that investors have to equity-account for investments in associates in their consolidated financial statements and in their separate financial statements. It would be more helpful if this paragraph could clarify that an investment has to be equity accounted:

- in the consolidated financial statements if those are prepared, or
- in the separate financial statements where an investor is not preparing consolidated financial statements.

Paragraph 11. This provides guidance on the accounting treatment that should be applied when an investor ceases to have significant influence but retains its interest in the associate. The guidance does not deal with the treatment of the disposal or partial disposal of an associate. We believe the revisions to IAS 28 should provide guidance on the treatment to be applied when an associate is sold or partially sold.

Paragraph 16A. This paragraph states that a group's interest in an associate is the aggregate of the holdings of the parent and its subsidiaries, excluding those held by minority interests of subsidiaries. Paragraph 22 also defines the investor's interest in an associate in connection with the treatment of losses. The definition used in paragraph 22 should be altered to make it clear that this definition applies only when losses are being considered.

Paragraphs 18 and 19. These paragraphs set out the guidance dealing with associates' reporting dates. We believe the guidance should specify that opening retained earnings and the comparatives should be adjusted when an associate changes its reporting date to be consistent with the investor or if not, additional disclosures should be given.

Paragraph 22B. This states that an investor recognises its shares of the losses of an associate when its interest in the associate has been reduced to nil only to the extent the investor has incurred obligations. We believe this paragraph should refer to both legal and constructive obligations.

Paragraph 24A. Since "separate financial statements" are defined in IAS 27 to include financial statements of a parent entity which does not prepare consolidated financial statements as per paragraphs 8 and 9 of IAS 27, this could mean that certain associates are not equity accounted in any financial statements if the investor is a parent entity which does not prepare a consolidated financial report. Paragraphs 29, 30 and 33 of IAS 27 would require investments in associates to be accounted for at cost or in accordance with IAS 39 in the separate financial statements.

Paragraph 24A should be amended to apply only where the investor prepares consolidated financial statements in addition to the separate financial statements.

Paragraph 24B. This should be amended to delete the words “that purport”.

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?

Yes.

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

Response to a) No. This proposal is inconsistent with paragraph 31 which states that 'dilutive potential ordinary shares shall be deemed to have been converted …at the beginning of the period' The examples in the Appendix do not form part of the proposed standard and are at present inconsistent with the requirements of the proposed standard. The number of reporting periods (be it half-yearly or quarterly or monthly) in the financial year should not influence the measurement basis of EPS or any other measurement basis in the annual financial statements. As illustrated in example 7, it does not aid comparability if the year-end denominator is less than the denominator used in the final quarter because a different measurement basis has been applied to the full year calculation.

We therefore believe that the calculation of potential shares (warrants) in Example 12 of the Appendix is incorrect and should be reworked as set out below:

Full year 20X1 - Diluted EPS calculation

The incremental number of shares for warrants is stated as 27,884. This weighting calculation as indicated above is incorrect. The correct figure should be 14,913 as calculated below:

Warrants to buy 600,000 shares at 55 were outstanding at the beginning of the year on 1 January 20X1. These warrants were all exercised on 1 September 20X1. Hence, they were outstanding for eight (8) months of the financial year. The average share price for the period the options were outstanding is calculated by reference to the weighted average market prices of the shares outstanding as follows:

First quarter = 49
Second quarter = 60
1 July to 1 September = 65

Therefore, weighted average is = $\frac{49 \times 3 + 60 \times 3 + 65 \times 2}{8} =$ 57.13

Deemed number of shares at full price = 600,000 x 55/57.13 = 577,630

Deemed issued at nil price = 600,000 – 577,630 = 22,370

Therefore, the incremental number of shares for warrants outstanding for 8 months is 22,370 x 8/12 = 14,913, that is, weighted for the portion of the period during which they were outstanding as set out in paragraphs 31 and 32.

Response to b) No. This proposal is inconsistent with paragraph 47 which states 'if the condition is based on an average of market prices over a period of time, the average for that period is used'. The number of reporting periods (be it half-yearly or quarterly or monthly) in the financial year should not influence the measurement basis of EPS or any other measurement basis in the annual financial statements. Taken alone this statement is confusing because statements a) and c) in question 2 above naturally require the interim average market prices to have been used. If this statement is read alone there should be no difference in averaging market prices over the year to date and averaging market prices of interim periods.

Response to c) No. This proposal is inconsistent with paragraph 45 which states that 'contingently issuable shares are included from the beginning of the period' and 'if the conditions are not met, the number of contingently issuable shares included in the diluted earnings per share calculation is based on the number of shares that would be issuable if the end of the period were the end of the contingency period'. Taken together these two statements imply that the calculation should be done independently depending on whether the contingency conditions are met at the end of the interim reporting period or at the end of the year to date reporting period. It would not be correct to calculate the weighting for the year to date reporting purposes based on the weighted average of the interim figures. We therefore believe that the calculation of contingent shares in Example 7 of the Appendix is incorrect and should be reworked as set out below:

Example 7 – Contingently issuable shares

Diluted earnings per share denominator:

Retail contingency

The weighted average number of shares for the retail contingency figure under the full year column should read 10,000 and not 6,250. It is not simply an average of the cumulative weighted average number of retail contingency shares outstanding at end of each quarter as set out in calculation (e). This is because 10,000 shares were issued at various dates (5,000 on 1 May and 5,000 on 1 September) during the year and should be weighted by reference to these dates from the beginning of the period in accordance with paragraph 45.

Proof:	Full year
Basic EPS – retail contingency	5,000
Diluted EPS – retail contingency 10,000 outstanding for 4 months and 5,000 outstanding for 4 months 10,000 x 4/12 + 5,000 x 4/12 =	5,000
Total for diluted EPS	10,000

Earnings contingency

Similarly the weighted average number of shares for the earnings contingency figure under the full year column should read 900,000 and not 300,000. This is because the conditions for issuing 900,000 contingently issuable shares were deemed to have been met by the year end and, therefore, should be included from the beginning of the year for diluted EPS calculation in accordance with paragraph 45.

As a result of the above changes, the denominator of the diluted weighted average number of shares for the full year should be 1,000,000 + 10,000 + 900,000 = 1,910,000. The diluted earnings per shares for the full year should be 2,900,000/1,910,000 = 1.52.

Other comments on IAS 33

Guidance on calculating profit or loss from continuing operations There is currently no guidance given on how to calculate profit or loss from continuing operations. Guidance on the allocation of taxation and interest between continuing and discontinuing operations for example would be useful and would aid comparability.

Paragraph 65. This permits an entity to disclose amounts per share using a reported component of the income statement other than one required by the standard. There is no requirement to reconcile the component used to the one required by the standard. We recommend that such a reconciliation should be given since the reported component of income could be a before tax component but the one required by the standard is an after tax component. The reconciliation would aid transparency and avoid the need to indicate whether the numerator(s) is or (are) determined on a pre or post tax basis.

Paragraph 65. This paragraph also permits an entity to disclose amounts per share using a component of income that is not reported as a line item in the income statement. In that situation, the proposed standard requires a reconciliation of the component used to any line item in the income statement. We recommend that the component of income used in the numerator should be reconciled to the component required by the standard and not to any line item reported in the income statement.

Paragraph 65. This paragraph should specifically state that additional earnings per share computations should be presented on a consistent basis over time.

The IASB should consider whether the proposed standard could include guidance on other per share measures and their use, for example cash flow per share and net assets per share. This would aid comparability in industries where other per share data is frequently given and used as an important indicator. For example, the guidance could state that the denominator should be calculated in accordance with the standard and the numerator reconciled to or clearly identified as a line item in the key performance statements.

The IASB should address the use of alternative and sometimes mis-leading presentation of amounts per share data given in the Operating and Financial Review ('OFR') and financial statements. This issue should be addressed but should be addressed in an OFR/ MD&A project rather than in IAS 33.

Transitional arrangements Additional guidance is needed to clarify that comparatives should be adjusted if application of a new standard changes the historical basis for calculating Earnings per Share ('EPS'). For example, guidance should be given that the adjustments required for preference shares set out in paragraphs 13-16 and weighting of interim periods rather than year-to-date periods could result in changes to the comparatives. A change in the basis of calculation on introduction of the new standard should be accounted for by restating the comparative figures for the preceding period and disclosing the effect of the adjustments on the EPS figures previously disclosed.

Examples We recommend that example 12 should be expanded to show year-to-date earnings per share figures at quarter 2 and quarter 3.

Appendix B. It would be helpful to include a comprehensive disclosure example that covers, for example, the requirements of paragraph 65.

IAS 40, Investment Property

Question 1

Do you agree that the definition of investment property should be changed to permit the inclusion of a property interest held under an operating lease provided that:

(a) the rest of the definition of investment property is met; and
(b) the lessee uses the fair value model set out in the IAS 40, paragraphs 27-49?

Yes.

Question 2

Do you agree that a lessee that classifies a property interest held under an operating lease as investment property should account for the lease as if it were a finance lease?

Yes.

Question 3

Do you agree that the Board should not eliminate the choice between the cost model and the fair value model in the Improvements project, but should keep the matter under review with a view to reconsidering the option to use the cost model in due course?

Yes.

Other comments on IAS 40

Paragraph 17/18. Transaction costs (paragraph 17) has the potential to be considered the same as "directly attributable costs" (paragraph 18) since the term "transaction costs" is not defined in IAS 40. We believe that the use of these different terms is confusing and requires consistency by either: (1) substituting transaction costs in paragraph 17 with directly attributable costs or (2) including an additional definition for transaction costs with examples of such costs, given that the term has the potential to be broadly interpreted.

Paragraph 20. We recommend the inclusion of a definition for start-up costs, along with examples of such costs, to help avoid inconsistencies in what costs are regarded as start-up costs.

Deferred taxation on investment properties The Board needs to revisit IAS 12 and SIC-21 at the same time as revising IAS 40. We do not believe it is appropriate to split the revaluation of a single composite investment property of land and buildings into two components and provide for deferred tax differently to the two elements: land at capital gains tax rates and buildings at income tax rates.

Revaluations are based on current market prices and thus deferred tax on both investment property land and buildings should be based on the (capital gains) tax rates that would be applied if the asset were to be sold at that amount at the balance sheet date.

Fair value of lease liabilities Where a company uses the fair value model for a leased asset which itself is held under a lease from a third party, we believe that it is not appropriate to carry that liability on an amortised cost basis. The standard should be amended to require the same basis to be applied to both leased assets and liabilities, where the entity adopts the fair value model, to avoid a mismatch of related gains and losses that will lead to the misstatement of net assets as well as net income.

Amendments to IAS 12

Paragraph 81(i). In the first line, replace “discontinued” with discontinuing.

Amendments to IAS 20

Paragraph 23. This paragraph states that the benefit of government loans at nil or low interest rates is not quantified by the imputation of interest. However, according to IAS 39-IGC 66-3, nil or no interest loans should be recognised at inception at the present value of the future payments, discounted using the market interest rates for similar loan. Since IGC 66-3 does not distinguish between government and non-government loans, and government loans are not scoped out of IAS 39.1, we suggest the IASB clarify this in revising IAS 20.

Amendments to IAS 34

Appendix B. With the abolition of LIFO in IAS 2, the Board should delete the example at paragraph 27 of IAS 34 and the references to LIFO in Appendix B, para 25 and Appendix C, para 1 of IAS 34.

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If you have any questions in relation to this letter please do not hesitate to contact Jochen Pape , Chair of the PwC Global IAS Board (49 211 981 2905) , or Ian Wright (44 207 804 43300).

Yours faithfully

PricewaterhouseCoopers