Project	**CONCEPTUAL FRAMEWORK: THE REPORTING ENTITY**
Topic	**Revised Project Timeline**

Introduction

1. At the October 2010 joint Board meeting, the staff presented a summary of the comments received on the Exposure Draft, *Conceptual Framework for Financial Reporting: The Reporting Entity* (the 2010 ED). The Boards agreed with the staff's list of issues to be discussed at future meetings but asked the staff to prepare a paper that discusses the time required to addresses these issues and the revised target issue date of the final chapter.

2. The objective of this paper is to discuss the revised project timeline for the reporting entity phase of the conceptual framework project. In the first half of this paper, the staff will discuss the two significant issues that seemed potentially troublesome when they came up at the October joint meeting, namely (a) the entity versus proprietary perspective and (b) the requirement for combined financial statements. In the second half of this paper, the staff will discuss the alternatives of the revised project timeline.

Potential Issues for Further Discussion

Entity versus Proprietary Perspective

3. At the October 2010 joint Board meeting, some Board members were concerned that the 2010 ED did not discuss the entity theory and the proprietary theory (that is, the perspective from which financial statements are prepared).

Proposal in the PV

4. In the Preliminary Views (PV), *Conceptual Framework for Financial Reporting: The Reporting Entity,* the Boards indicated a preference of the entity perspective but also noted that the Boards have not rejected the parent company approach in its entirety.

5. A majority of respondents who commented on this issue agreed with the Boards' preliminary view that consolidated financial statements should be presented from the perspective of the group reporting entity.

6. A few respondents emphasized that presentation from the perspective of the group reporting entity is the only realistic option. In these respondents' view, the parent company's shareholders are only one (albeit important) group of capital providers and preparing consolidated financial statements from their view would rob the financial statements of neutrality. One of these respondents noted that having a broad range of users is the essence of general-purpose financial reporting.

7. On the other hand, several respondents noted that reporting financial results from the perspective of the parent company shareholders is the most effective and efficient means to communicate decision useful information to capital providers, and is therefore the approach most consistent with the objective of financial reporting. They did not explain, however, how those statements would differ from statements prepared under an entity perspective.

8. Several other respondents noted that the Boards have not adequately discussed or debated this issue to justify their conclusion.

Proposal in the 2010 ED

9. Many respondents stated that there is no discussion in the 2010 ED regarding the perspective from which financial statements should be presented. These respondents noted that the PV proposed that the entity perspective be adopted.

10. A few respondents who commented on this issue supported the entity perspective, and a few other respondents who commented on this issue supported the proprietary perspective or the parent company approach. Several respondents commented that this issue has not been fully debated and, therefore, they could not make a decision.

11. A few respondents who commented on this issue noted that the 2010 ED seemed to support the entity perspective, but that this was not clear. One respondent asked the Boards to provide the reasons for having deleted the discussion of the entity perspective and whether the Boards intend to retain the preference for the entity perspective as proposed in the PV.

Chapter 1 of the Conceptual Framework for Financial Reporting

12. Paragraph BC1.8 of the Conceptual Framework for Financial Reporting states:

> Some respondents to the exposure draft said that the reporting entity is not separate from its equity investors or a subset of those equity investors. This view has its roots in the days when most businesses were sole proprietorships and partnerships that were managed by their owners who had unlimited liability for the debts incurred in the course of the business. Over time, the separation between businesses and their owners who had unlimited liability for the debts incurred in the course of the business. The vast majority of today's businesses have legal substance separate from their owners by virtue of their legal form of organization, numerous investors with limited legal liability and professional managers separate

from the owners. Consequently, the Board concluded that financial reports should reflect that separation by accounting for the entity (and its economic resources and claims) rather than its primary users and their interests in the reporting entity.

Staff Analysis

13. The staff thinks the Boards should not discuss the perspective from which financial statements are presented in the reporting entity chapter (in addition to what is discussed in this paper) for the following reasons:

    (a) The choice of the perspective does not affect the boundaries of the reporting entity. That is, the perspective is applied once the boundaries of the reporting entity are determined.

    (b) There is no widely accepted definition for each of the perspectives. Time spent discussing labels that refer to vague concepts would not be productive.

    (c) Paragraph BC1.8 explains clearly enough that statements are prepared from the perspective of the entity. There is no reason to readdress that issue in the reporting entity chapter.

14. Accordingly, the staff recommends that the Boards not address the issue of the entity versus proprietary perspective in the reporting entity chapter.

Question for the Boards
1. Should the issue of the entity versus proprietary perspective be addressed in the reporting entity chapter?

Combined Financial Statements

15. At the October 2010 joint Board meeting, some Board members raised concerns that the 2010 ED was not clear about when it would be appropriate to prepare combined financial statements.

Proposal in the 2010 ED

16. Several respondents welcomed the Boards' intent to discuss combined financial statements in the conceptual framework. Another respondent noted that combined financial statements should be discussed at the standards level. Yet another respondent noted that combined financial statements are special purpose financial statements.

17. One respondent noted that it was unclear whether combined financial statements should include all commonly controlled entities. This respondent suggested that that should not be the case.

18. Many respondents disagreed with the Boards' proposal that combined financial statements should be restricted to the combination of entities under common control. These respondents noted that this approach seemed to be inconsistent with the broad description of a reporting entity and that the Boards have not provided enough explanation for this restriction.

19. In the view of the respondents who disagreed with the Boards' proposal, combined financial statements could also be appropriate for some groups where there is no control relationship between any of the entities of the group. These respondents noted that, in several countries, combined financial statements are prepared for specific structures of groups of mutual banks.

20. A few respondents noted that it was not clear whether the proposal meant to address situations where there is no entity identifiable as the controlling entity.

21. One respondent noted that combined financial statements may provide useful information about entities under common management in addition to entities under common control. Another respondent noted that it may be appropriate to restrict the use of combined financial statements to a set of commonly-directed entities to ensure consistency with the objective of general purpose financial reporting.

22. Another respondent noted that the 2010 ED states that combined financial statements may be appropriate for entities under common control, whereas

paragraph 810-10-55-1B of the *FASB Accounting Standards Codification*™ states that combined financial statements may also be appropriate for entities under common management. This respondent asked the Boards to resolve this inconsistency.

23. A few entities asked the Boards to clarify whether, to the extent one of the combining entities itself controls one or more entities, the combined financial statements should include all of those controlled entities.

Staff Analysis

24. While most issues raised by constituents seem to be standards-level issues, one potential issue for discussion at the conceptual level is whether the Boards should restrict the use of combined financial statements to entities that are under common control. As noted above, many respondents agreed that common control would be one reason for justifying two or more entities to prepare combined financial statements but questioned whether that should be the only reason.

25. One solution to this issue might be that the Boards revert to the description of a reporting entity. That is, the Boards could state in the reporting entity chapter of the conceptual framework that two or more entities may prepare combined financial statements if those entities, as a group, meet the description of a reporting entity and possess the features of a reporting entity. Under this solution, any further restrictions to the use of combined financial statements would be determined at the standards level.

26. Unless the Boards decide to retain the proposal in the 2010 ED and restrict the use of combined financial statements to entities that are under common control, the staff thinks the Boards will need to spend significant time to develop concepts related to combined financial statements. Staff members have mixed views regarding whether the Boards should do so.

Question for the Boards
2. Should the Boards restrict the use of combined financial statements to entities under common control?

Alternatives of the Revised Project Timeline

27. The staff considered four alternatives of the revised project timeline. The differences among the alternatives arise because of the two issues discussed earlier in this paper. These alternatives can be summarized as follows:

	Alternative A	**Alternative B**	**Alternative C**	**Alternative D**
Redeliberations of the 2010 ED	December 2010 -March 2011	July 2011 -November	(combined with the 2011 ED)	December 2010 -March 2011
Final chapter based on the 2010 ED	**June 2011**	**March 2012**	(combined with the 2011 ED)	**June 2011**
Further discussions on the entity perspective or combined financial statements (or both)	N/A	N/A	July 2011 -September 2011	July 2011 -September 2011
Exposure Draft on the entity perspective or combined financial statements (or both) (the 2011 ED)	N/A	N/A	December 2011	December 2011
Comment period for the 2011 ED	N/A	N/A	January 2012 -April 2012	January 2012 -April 2012
Redebilerations of the 2011 ED*	N/A	N/A	July 2012 -September	July 2012 -September
Final chapter based on the 2011	N/A	N/A	**December 2012**	**December 2012**

*For Alternative C, the issues addressed would include issues addressed in the 2010 ED

Alternative A

28. Under Alternative A the Boards would not spend significant time discussing the two issues discussed earlier in this paper. It is based on the view that issues identified in the October joint Board meeting can be discussed in four Board meetings. Under Alternative A, the Boards would begin redeliberations in December 2010 and, as a result, the revised target issue date for Alternative A would be June 2011.

29. One of the advantages of Alternative A would be that the IASB would vote for the final chapter before the expected changes in Board members in June 2011. One of the disadvantages of Alternative A would be that both Boards have made

commitments to complete four major joint projects by June 2011 and that the Boards may not be able to work on the conceptual framework.

Alternative B

30. Alternative B is similar to Alternative A except that under Alternative B, the Boards would not begin redeliberations until July 2011, taking into account the Boards' priorities in other projects. As a result, the revised target issue date for Alternative B would be March 2012.

31. One of the advantages of Alternative B would be that the Boards would be committing to continue to work on the conceptual framework after the major commitment date of June 2011. However, disadvantages of Alternative B include delays in making progress in the conceptual framework and possible changes due to Board member turnover.

Alternative C

32. Under Alternative C the Boards would spend significant time discussing one or both of the two issues discussed earlier in this paper.

33. The Exposure Draft did not address the entity versus proprietary perspective[1], and it did not propose to specify a requirement for combined financial statements. If the Boards change their decisions on either of those two issues, the Boards would need to give constituents an opportunity to comment by issuing a revised Exposure Draft. If that is the case, the discussions should begin only after July 2011 and, as a result, the revised target issue date for Alternative C would be December 2012.

34. One of the advantages of Alternative C would be that the Boards would be committing to continue to work on the conceptual framework after the major commitment date of June 2011. However, disadvantages of Alternative C include

[1] One Board member pointed out in the October meeting that Chapter 1 addressed the entity perspective without naming it. Paragraph 12 of this paper quotes the relevant paragraph.

delays in making progress in the conceptual framework and possible changes due to Board member turnover.

Alternative D

35. Under Alternative D the Boards would address the same issues as in Alternative C but would issue two separate final chapters (or issue Chapter 2 in two parts).

36. The first document would be based on the 2010 ED and would have a target issue date of June 2011. Accordingly, this document would be the same as that published for Alternative A. The second document would be based on a yet to be issued Exposure Draft and would have a target issue date of December 2012.

37. One of the advantages of Alternative D would be that the IASB would vote for the first document before the expected changes in Board members in June 2011. When compared with Alternative C, the conceptual framework would be improved earlier. Moreover, issuing two documents may be preferable, particularly for discussing the entity versus proprietary perspective, because that discussion may be better positioned outside the reporting entity chapter.

Staff Recommendation

38. If the Boards think that they should not spend significant time discussing the two issues discussed earlier in this paper, the staff recommends Alternative A (target issue date of June 2011) because the conceptual framework would be improved earlier.

39. If the Boards think that further discussions are necessary for either of the two issues discussed earlier in this paper, the staff recommends Alternative D (the target issue date of June 2011 for the first document and the target issue date of December 2012 for the second document) because the conceptual framework would be improved earlier.

Questions for the Boards	
3.	Which Alternative do the Boards prefer?
4.	If the Boards prefer either Alternative C or D: (a) should the Boards spend significant time discussing (1) the entity versus proprietary perspective, (2) the requirement for combined financial statements, or (3) both? (b) do the Boards agree that the additional discussions for items in (a) need to be exposed for public comment?