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## DSR – öffentliche SITZUNGSUNTERLAGE

<b>DSR-Sitzung:</b>	<b>129. / 09.03.2009 / 15:45 – 16:45 Uhr</b>
<b>TOP:</b>	<b>04 – IAS 24 Related Party Disclosures</b>
<b>Thema:</b>	<b>Stellungnahme an den IASB</b>
<b>Papier:</b>	<b>04b Entwurf Stellungnahme DSR an IASB (ED amend IAS 24)</b>



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Berlin, 19 February 2009

Dear David,

**Exposure Draft 'Relationships with the State – Proposed amendments to IAS 24'**

We appreciate the opportunity to respond to the International Accounting Standards Board's Exposure Draft (ED) 'Relationships with the State – Proposed amendments to IAS 24'. This letter represents the view of the German Accounting Standards Board (GASB).

Regarding the IASB's proposal to exempt state-controlled entities from the disclosure requirements of IAS 24.17, we believe that the proposed exemption does not satisfactorily address the underlying issue, which is the identification of other state-controlled entities. Outlined below you will find two alternative proposals to deal with the issue.

As a result of our considerations we strongly support the Board's efforts to achieve an improved definition of related parties by a general restructuring and by deleting inconsistencies. However, we recommend to provide some detailing guidance as to how the term "significant voting power" shall be defined.

In addition, we have some other comments on the proposal(s) to amend IAS 24 – mainly to limit related party relationships generally to those having 'control' and 'joint control' character.

For detailed comments we refer to the appendix to this comment letter.

If you want to discuss any aspects of this letter in more detail, please do not hesitate to contact me.

Yours sincerely,

*Liesel Knorr*  
President



## APPENDIX

### Question 1—State-controlled entities

This exposure draft proposes an exemption from disclosures in IAS 24 for entities controlled, jointly controlled or significantly influenced by the state in specified circumstances.

Do you agree with the proposed exemption, and with the disclosures that entities must provide when the exemption applies?

Why or why not?

If not, what would you propose instead and why?

We do not agree with the proposed exemption and with the disclosures that entities must provide when the exemption applies because of the following reasons:

- 1) The proposed exemption does not satisfactorily address the main underlying issue state-controlled entities are frequently facing, which is the problem (if not the impracticality) to identify other state-controlled entities. In BC11 of the ED it is mentioned that the main alleviation for a state-controlled reporting entity would be, not “to identify every state-controlled entity”. However, the reporting entity may not even be in a position to identify any state-controlled entity being a related party.
- 2) On the other hand, we understand that a reporting entity based on para. 17A of the ED will be exempted from the disclosure requirements of IAS 24.17 even if this reporting entity is able (without unreasonable burden) to fully comply with IAS 24.17.
- 3) Further, we are of the opinion that the difficulty to identify related parties is not an issue pertaining solely to state-controlled entities, but that it can be evident for all related party environments (eg complex group structures and related party relationships involving persons (individuals)).

Instead we propose to address the issue and the above concerns according to either of the following two alternatives:

#### Alternative 1

In a first step reporting entities shall be required to make a qualitative statement whether transactions have been made between related parties with a “best endeavours clause”. According to this clause the disclosure will not be required if the reporting entity, despite using its best endeavours, is unable to obtain the necessary information (however, applying the “best endeavours clause” would need to be disclosed).



In a second step a reporting entity shall be required to quantify the information provided in accordance with step 1 and in line with IAS 24.17 – also with a “best endeavours clause”, accordingly.

Both requirements (according to steps 1 and 2) would need to be met irrespective of the nature of the related parties (eg whether state-controlled entities are involved or not).

### Alternative 2

No exemption from the disclosure requirements of IAS 24.17 shall be provided at all for a reporting entity in relation to

- a state that has control, joint control or significant influence over the reporting entity; and
- another entity that is a related party because the same state has control, joint control or significant influence over both the reporting entity and the other entity.

The main reason for alternative 2 is the fact that we consider an exemption as lined out in para. 17A of the ED not to be practicable in the light of the disclosure requirements of para. 17B (b) of the ED considering the problem (if not the impracticality) to identify other state-controlled entities as described above.

Further, the disclosures according to IAS 24.17 shall be required for relationships based on control or joint control, only. Thus, relationships based on significant influence and significant voting power shall not lead to the aforementioned disclosures. The rationale behind this approach is that under normal circumstances significant influence and significant voting power do not provide sufficient influence to enter into transactions with the reporting entity which are not based on an arm's length basis. Consequently, there is no need to inform the user of the financial statements as to how these parties affect the reporting entities' financial position and profit or loss by transactions and outstanding balances in the context of IAS 24.

Compared with the ED amend IAS 24 (February 2007), the definition of state-controlled entities proposed in IAS 24.17A (a) and (b) per ED amend IAS 24 (December 2008) now also considers joint control (in addition to control and significant influence as proposed in 2007). In this context, we suggest to the IASB that it fully considers any consequential changes stemming from ED 9 *Joint Arrangements* and the respective standard expected to be issued in Q2 / 2009.



**Question 2—Definition of a related party**

The exposure draft published in 2007 proposed a revised definition of a related party. The Board proposes to amend that definition further to ensure that two entities are treated as related to each other whenever a person or a third entity has joint control over one entity and that person (or a close member of that person's family) or the third entity has joint control or significant influence over the other entity or has significant voting power in it.

Do you agree with this proposal?

Why or why not?

If not, what would you propose instead and why?

We generally agree with the proposal of the definition of a related party, but would like to add the following comments:

- 1) In (b) (vii) and (x) of the definition of a related party as suggested in the ED, a related party relationship will be established in case there is significant voting power in an entity. However, in case there will be significant influence over that entity, a related party relationship will not be established. In this context we wonder what is the rationale to define a related party on the basis of a relationship presumably providing less influence (ie significant voting power), but not on the basis of a relationship providing a higher level of influence (ie significant influence)?
- 2) We further propose defining the term "significant voting power". Although the term is used in the current text of IAS 24 and in a number of other standards, it is not a defined term in IFRS. This creates inconsistencies and divergence in practice.

It might not be necessary to define the term based on bright lines, but a rebuttable presumption when significant voting power needs to be assumed would be a great achievement. The term should specifically be set in relation to the term "significant influence".

**Question – Definition of a related party**

Do you have any other comments on the proposals.

We have the following comments on the proposals:

- First of all, we are disappointed that the IASB did not follow the arguments brought forward in our comment letter of May 2007 with respect to the definition of the term "related party". We, again, suggest reconsidering fundamentally the current as well as the proposed definition of a related party relationship. Both the current and the proposed definition assume that significant influence is enough to influence transactions between the reporting entity and the related party in a way



that the transactions would not have entered into or at conditions different from market rates. We doubt whether this is true. Significant influence is defined as the power to participate in the financial and operating policy decisions of an entity but not as control over these policies. We are of the opinion that this power is not enough to influence transactions of that entity in the aforementioned sense. As a result the definition should be limited to those relationships which are of (joint) control character. This would not only lead to a significant alleviation for preparers, but also increase the explanatory power of the reported disclosures as many irrelevant disclosures would be eliminated. Hence, users would benefit from this limitation, too.

- Our understanding about the proposed amendment to the definition of close family members (ED amend IAS 24 – February 2007) is that the definition is extended too far. We are of the opinion that the same fundamental idea, as mentioned above, should be applied to the question whether all close family members should be regarded as related parties. We believe that the current and even more the proposed definition are much too far reaching. A limitation to a smaller group of dependants, determined on the basis of a clear underlying principle, would be helpful for preparers and users.
- With regard to IAS 24.20, we suggest clarifying whether or not dividend payments are part of related party transactions as this is a frequent question in practice. We are of the opinion that dividend payments do not meet the requirement of being a transfer of resources, services or obligations between the reporting entity and the related party.

Further comments relate to the definition of a “related party” as follows:

- The definition of a “related party” is worded in para. 9 (a) of the ED as follows: “A person or a close member of that person’s family is ...”. We consider this wording not to be clear since in our understanding the following is meant: “If a person
  - (i) is a member ...,
  - (ii) has control ...; or
  - (iii) has joint control, ...,the person and all close members of that person’s family are related to the reporting entity.” If our understanding is correct, we suggest to the IASB the clarification of the wording.
- According to para 9 (a) (i) of the ED, a person or a close member of that person’s family is related to a reporting entity if that person is a member of the key management personnel of a parent of the reporting entity. The respective wording in IAS 24.9 (d) makes reference to the parent of the reporting entity (“... its parent;”). In case the IASB still intends to define the key management personnel or a close member of that person’s family of the immediate parent of the reporting entity to be a related party, we recommend clarifying the wording accordingly.



- The term “related party” as defined in IAS 24.9 (f) explicitly states that the relationship between the two parties mentioned in that paragraph may be established either “directly or indirectly”. However, the definition in para. 9 (a) of the ED does not include such a clarifying comment. We suggest also using the term “directly or indirectly” in the new definition for clarity purposes.
- The definition of a “related party” in para. 9 (b) (iii) of the ED states “both entities are joint ventures of a third party.” In this context we propose:
  - to investigate whether the term “party” may need to be replaced by the term “entity”, which we believe to be appropriate;
  - to investigate whether the term “entity” may be used inconsistently across IFRS (eg in IAS 24 the term would exclude persons (individuals), whereas in IAS 32, in the definition of a financial instrument, it would be a generic term for both entities and persons (individuals)).
- In para. 9 (b) (ix) of the ED two requirements are listed which must be met to establish a related party. In this context, (A) and (B) are used as list elements, which is confusing since (A) and (B) inappropriately may be understood to be two different parties. We suggest clarifying the wording.