

European Financial Reporting Advisory Group
13/14 Avenue des Arts
1210 Brussels
Belgium

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sent by e-mail to: commentletter@efrag.org

Grant Thornton International welcomes the opportunity to comment on the European Financial Reporting Advisory Group (EFRAG) Discussion Paper *The Conceptual Framework Starting from the Right Place?* (the Paper). We support the pro-active and other work of EFRAG and congratulate it on its substantial contribution to this important debate. Our views on a number of the issues raised in Paper are set out below.

We are also attaching for information our response to the International Accounting Standards Board (IASB) and Financial Accounting Standards Board (FASB) Preliminary Views, *Conceptual Framework for Financial Reporting: Objective of Financial Reporting and Qualitative Characteristics of Decision-Useful Financial Reporting Information* ("the Preliminary Views Document").

Should the framework be mandatory and, if so, for whom?

The answer to this question will to a large degree be a function of the objective of financial reporting and, by extension, the objective of the framework. We believe that the framework proposed in the Preliminary Views Document, with its emphasis on resource allocation decisions for investors and a narrowly defined group of creditors, is not well suited to entities that do not have public accountability. The recently issued Exposure Draft, *IFRS for Small and Medium-sized Entities* (hereafter the SME Exposure Draft), appears to lend support to that view. The SME Exposure Draft contains its own framework for other entities, complete with separate objective and qualitative characteristics, further suggesting that the conceptual framework does not apply to that audience.

We would prefer to see a common framework for all entities. The objective in the current proposal for the conceptual framework may be too narrow for that purpose. In our comment letter to the IASB, we suggested that the objective in the SME Exposure Draft would be a better fit as the objective of general purpose financial reporting. Were such an objective to be adopted, we would be more inclined to suggest that the framework should be mandatory and applied to all entities. Under the current proposal in the Preliminary Views document, we believe it should be mandatory only for entities with public accountability, if at all.

Are general purpose financial statements for all stakeholders a valid concept?

We agree with the tentative view that little or no evidence has been provided to justify the assertion that financial statements that meet the needs of investors and creditors will meet the needs of other user groups. We agree that further research in this regard is required. We do not, however, agree that the focus should be on the definition of homogenous categories of users with regards to their needs unless it is decided to adopt a proprietary perspective.

We believe that the entity perspective and general purpose financial statements for all stakeholders is a valid concept and should be a core feature of a conceptual framework. The core of an entity perspective is that there are certain commonalities in all financial statements based on accounting records, regardless of the type of entity. The common need of all users could be described in terms of a degree of transparency into the books of the reporting entity and thereby into the financial position of the entity, the operations of the reporting entity and the results of operations. Those common needs have been expressed in the objective in the SME Exposure Draft as: “information about the financial position, performance and cash flows of the entity that is useful for economic decision-making.” Under an entity approach, the content of the information in financial statements could be independent of the intended use by an unspecified user. We believe that this is the original meaning of the term general purpose financial reporting.

We acknowledge, however, the objective in the Preliminary Views document, with its focus on information about future cash flows to inform resource allocation decisions by investors and creditors, is de facto a proprietary perspective. The central argument for the proprietary perspective is that the content of the information should be dependent on the intended use of the information. Therefore, it is necessary to define a specific user.

It is not clear whether such financial statements should still be considered to be general purpose financial statements. The FASB and IASB have tried to make that case in the Preliminary Views document: nearly half of chapter one consists of arguments to establish that financial reporting based on a proprietary perspective still qualifies as general purpose financial reporting (paragraphs OB3-OB15). As we noted in our comment letter to the FASB and IASB, those arguments are to a large degree based on the unproven assertion that information that meets the needs of investors and creditors (narrowly defined) for resource allocation decisions will meet the needs of other users. If one accepts those arguments, then we believe that this will create a different meaning of the term general purpose financial reporting. If a proprietary perspective is adopted, then general purpose financial statements in the traditional sense may not be a valid concept going forward.

Do investors and creditors represent a homogeneous enough group to be chosen as primary users?

This question is only relevant if a proprietary perspective is adopted. Under a proprietary perspective we agree with the tentative view that it is necessary to define both the users and their needs. If an entity perspective is adopted, then we do not believe that it is necessary to designate primary users and the issue is debatable.

We do not agree with the tentative view that a clear definition of primary users of financial information and their needs has to be provided before revising the framework. We believe that it may be infeasible and probably unnecessary to specify the decision making need of users in advance. Even among homogeneous groups, such as equity investors, there are a multitude of valuation models and techniques for using financial information to assess future cash flows. Differences in expectations about those cash flows cause one investor to sell and another to buy an equity share at any given point in time. Without that diversity in expectations, financial markets could not function. Therefore, financial reporting that would lead to uniform resource allocation decisions by users may not be a realistic goal. Under an entity perspective, however, we believe that it is not necessary to identify a primary user. Consistent with the objective in the SME Exposure Draft, the focus of a framework would be on the content of the financial statements, and not on how they are used.

Do the users of financial reporting of different types of entity have similar needs?

We agree with the tentative view that it may be possible to extend the scope of the framework to non-profit oriented entities if an entity perspective is adopted. The common need of all users could be described in terms of a degree of transparency into the books of the reporting entity and thereby into the financial position of the entity, the operations of the reporting entity and the results of operations. For example, the objective of financial statements in the SME Exposure Draft may meet the needs of users of financial statements of non-profit oriented entities as well as profit-oriented entities of all sizes.

Do the users of financial reporting of small, large, listed and unlisted entities have similar needs?

Under a proprietary perspective, we consider that the needs of users of financial statements of larger, listed companies differ from those of smaller, unlisted companies. Shareholders in listed companies are constantly making resource allocation decisions. Thousands or millions of shares may be traded on any given day that markets are open. The users of smaller, unlisted companies make also make resource allocation decisions, but typically much less frequently.

Our answer may change if one adopts an entity perspective. We believe that under an entity perspective, the needs of users of general purpose financial statements of small, large, listed and unlisted companies are fundamentally the same. However, the costs and benefits of providing that information may not always be the same and should be taken into consideration by standard setters when establishing reporting requirements.

Do financial statements and other types of financial reporting have similar objectives?

We agree with the tentative views that it is necessary to determine what it meant by financial reporting before answering the questions in part 5. In our comment letter to the IASB on the Preliminary Views document, we did not agree with the Boards decision to defer defining financial reporting until later in the project. We therefore agree that it is necessary to define financial reporting before proceeding with the framework.

Depending on how financial reporting is ultimately defined, we agree that it is possible that there could be separate qualitative characteristics. We also agree that financial statements and financial reporting could require separate treatment and not necessarily in the same conceptual framework.

Can all kinds of financial reporting be dealt with by the same framework?

We believe that this question can only be answered once financial reporting has been defined.

Do financial statements and other types of financial reporting have similar qualitative characteristics?

We believe that this question can only be answered once financial reporting has been defined. However, we agree with the tentative view that the qualitative characteristics of financial reporting, such as management information, may not have the same qualitative characteristics as financial statements.

If you have any questions on our response, or wish us to amplify our comments, please contact our Director of International Financial Reporting Standards, Mr Andrew Watchman (andrew.watchman@gtuk.com or telephone +44 (0) 207 7391 9510).

Yours sincerely,



April Mackenzie
Executive Director of Public Policy
Grant Thornton International