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

20 March 2009

Exposure Draft ED10, Consolidated Financial Statements

Dear Sirs

The Roche Group has a turnover of CHF 46 bn. a year (EUR 29 bn.) derived from our worldwide healthcare business - pharmaceuticals and diagnostics - and employs over 80,000 worldwide. We have a market capitalisation (end 2008) of CHF 141 bn. (EUR 95 bn.) We have been preparing our consolidated financial statements according to IFRS/IAS since 1990 and therefore have a substantial interest in how these will develop.

We approve of the IASB's efforts respond to the needs of users that the financial crisis has brought to light, and the additional disclosures suggested – with some adaptations described below – would help in this respect. However, we have difficulty in discerning in the proposals on consolidation any significant improvement in the current guidance in IAS 27 and SIC 12 and think that some more work is necessary before a revision in this regard is ready. We therefore recommend the IASB to press on with the supplementary information for users as quickly as proposed but to undertake more investigation and consideration before finalising the consolidation requirements. Detailed comments are to be found in the appendix to this letter.

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Sincerely,

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Appendix: Detailed comments on ED10, Consolidated Financial Statements.

1- General

It appears to us that more work and field testing are required to ensure that implementation of the future standard will not result in changes in the scope of consolidation which would reduce the usefulness, relevance and quality of the information provided to users. The Board should investigate more thoroughly what the needs of active users of consolidated financial statements are in this respect and, after reflecting these in their proposals, explain why financial reporting would be more useful to users as a result. The Board should therefore make the revisions in two steps:

- 1. the revised disclosure requirements (subject to the adaptations indicated below) as quickly as planned;
- 2. the scope of consolidation in a the second step which would require more time to investigate and reflect user needs but still achievable before 2011.

2- Answer to the Invitation for Comment

2.1 Is the control principle as articulated in the draft IFRS an appropriate basis for consolidation?

We approve of the definition of a single control principle to be applied to all entities today included in the scope of IAS 27 and SIC 12 and agree with the principle being based on the three identified elements, power, returns and the link between them. However, we have concerns about the proposals as the guidance provided does not seem to us in all aspects the best possible application of the core principle:

--- Beyond paragraphs 19 and 20 which develop the return criterion as part of the core principle and paragraph 33 which relates to structured entities, there is no guidance referring to the assessment of returns or of the influence the power of the reporting entity may have on the returns.

--- We approve of the efforts made to ensure that the future standard would be principle-based. We note however three areas where conclusions seem to be pre-defined:

- B13 (a) and (c) describe elements of facts and circumstances which taken in isolation from all other facts and circumstances would designate situations in which potential voting rights would give the reporting entity power; we disagree with not leaving room for judgement in the assessment of power; we believe that an in-substance analysis is necessary in all circumstances as described in B13 (b).
- B11 sets a rebuttable presumption, i.e. a predefined conclusion in every situation of dual role as agent and investor. We believe the analysis and exercise of judgement should be more open. All facts and circumstances ought to be taken into consideration in the consolidation decision.
- Paragraph 33 states a likelihood based on the significance of returns; it is difficult though to identify the role this likelihood is supposed to play. In addition, we do not see why this likelihood would play a role in structured entities and not in others.

- --- The standard is clear in defining power as “the ability” to direct the activities of the entity. There is, however, no reasoning of what ability the entity should have at the reporting date, at the time control needs to be assessed if the continuous assessment principle is to be effective. We note that the ability may designate:

- the ability to direct if I so wish (a passive shareholder being one that has decided against exercising its ability);
- the ability to direct because I have the ability to make a decision that would enable me to direct (the holder of a call option having to decide to exercise its option).

We believe that the future standard will be consistent if the ability to direct the activities of the entity is not determined taking into account what the entity might have done but has not done when there is a difference in economic substance between one situation and the other, in terms of both power and returns.

--- The Board has re-affirmed that financial reporting is useful to users when it helps capital providers to assess the future cash flows of an entity. It is relatively easy to understand how the return element of the control definition plays a role in making financial statements useful to capital providers. It is not so easy to explain how the power element makes such a big difference, especially if power is defined as never being shared. We believe that the IASB should fully develop its reasoning on this question, one to which preparers, auditors and enforcers could relate when assessing a difficult set of circumstances. In making cash flow predictions users need to rely on assumptions, and if rational behaviour has to be one of the assumptions used, we see that the power element is necessary to ensure that the entity is not playing against its interests. If that is the reasoning of the Board, though, we do not understand why the Board excludes shared control. As we have already indicated, shared control is control and the entity does have the power to ensure that no decision is made which would not be in its best interests. A partner in a joint venture is likely to have been chosen (exercise of power by the reporting entity) because its interests are congruent with the interests of the reporting entity, not contrary to them, so that shared control within the joint venture would not end up being a series of compromises, i.e. a series of half reasonable economic behaviours. We cannot see why the Board would exclude consolidation of a joint venture with 50% of shared control interests.

2.2 Are potential voting rights dealt with adequately?

We believe that there may be circumstances where potential voting rights are an indicator of an entity having the power to direct the activities as if it was already the holder of the voting interests. We therefore agree with the Board that care in the analysis is required – and understanding of the rationale of the transaction leading to these potential voting rights is needed – before concluding whether the reporting entity has control over an entity. We agree with B13 (b) because it calls for the necessary analysis in substance. We would also agree that where there are potential voting rights and evidence of effective control by the entity (both power and returns), circumstances trigger consolidation and agree with the spirit of BC84. However, we have areas of disagreement with the position the Board has taken in this area:

- We have already indicated why we disagreed with B13 (a) and (c);
- BC 85-87 adds to the proposed guidance although it is placed in the basis for conclusions (where requirements are supposed to be explained, not stated);
- We believe that non exercisable instruments cannot be regarded as "potential" voting rights at the balance sheet date, i.e. are contrary to the continuous assessment principle.

2.3 Are the conclusions drawn by the IASB on the dual role as an investor and an agent appropriate?

We agree with the IASB that the two positions – investor and agent – need to be considered in aggregate. We believe – as already indicated – that there should not be any room for a rebuttable presumption in the final standard. We believe that the circumstances should not be assessed from the power criterion only and that the significance of the exposure of the reporting entity to the variability of returns of the other entity should have a weight in the decision whether to consolidate. Furthermore we understand that B11 does not apply to structured entities because B11 deals with voting rights and that a structured entity is one to which paragraphs 23-29 do not apply. The final standard should be clear on this issue.

2.4 Is the definition of a "structured entity" necessary and appropriate? Are the requirements regarding the assessment of control in structured entities appropriate?

We understand the definition as ensuring that no entity falls out of scope and therefore support it. We also see the usefulness of the definition in the Board's attempt to identify the need for useful disclosures. We however believe that the lay-out of the standard as well as the divide between standard and guidance need to be revised:

- the standard seems to introduce two sets of distinct requirements, one for entities directed by way of voting rights, the other for structured entities;
- because of insufficient cross-referencing between the standard and the guidance, it is difficult to understand whether the guidance applies generally or to a sub-set of entities;
- both power and returns should be clearly assessed, and assessed in the same fashion – though on the basis of different sets of circumstances - whatever the entity.

As indicated earlier in our response, we believe that the exercise and outcome of past power should be taken into consideration in the analysis of whether a structured entity is consolidated.

2.5 Are the disclosure requirements likely to meet users' needs?

We support the IASB in its efforts to respond positively and swiftly to the needs of supplementary information that the financial crisis has enlightened. However, we believe that no disclosure can compensate for inadequate accounting. We therefore believe that it is of the utmost importance that the basis for consolidation that the IASB retains in the final standard is at least as sound as the existing IAS 27/SIC 12 requirements. Moreover we do not support disclosures which seem to be designed to help users to second guess management in its consolidation decisions.
We therefore:

- support the disclosure requirements related to restrictions on consolidated assets and liabilities and interests that the non-controlling interests have in the group's activities (B35-37),
- support the disclosure requirements related to involvement with unconsolidated structured entities and associated risks to the extent it does not replicate or duplicate information required in other standards (B38-B47), though we think that the final standard should make it clear that the requirement relates to "sponsored" entities rather than to e.g. structured entities set up by suppliers on which the reporting entity has little if any information.
- disagree with the disclosure requirements related to the basis of control and the impact of those decisions on the financial statements of the entity. We believe these disclosures are unnecessary if the final standard on consolidation is robust and likely to suggest uncertainty and hence suspicion or lack of confidence by users (B32-B34).