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IASB considers ‘what is a reporting entity’?

On 29 May 2008, the International Accounting Standards Board (IASB) published a Discussion Paper (DP) **Preliminary Views on an improved Conceptual Framework for Financial Reporting – The Reporting Entity**. This DP is the next step in the joint project with the US Financial Accounting Standards Board (FASB) to develop a consistent conceptual framework, and considers issues for the purposes of developing a reporting entity concept for inclusion in that conceptual framework.

The Boards are seeking comments by 29 September 2008.

While the DP presents the Boards’ preliminary views on some key issues related to control, work also continues on specific standards, most notably the Consolidations Project.

Definition of a reporting entity

Other components of the Conceptual Framework project have concluded that the objective of financial reporting is to provide financial information about the *reporting entity* that is useful to present and potential investors, lenders and other creditors in making decisions in their capacity as capital providers. To build on that principle, the Boards consider that it would be useful for the Conceptual Framework to broadly describe (rather than precisely define) what are the defining characteristics of a reporting entity.

The DP proposes that a reporting entity should be described as ‘a circumscribed area of business activities of interest to present and potential equity investors, lenders and other capital providers’. It also suggests that a reporting entity should not be limited to business activities that are structured as legal entities – so that sole proprietorships, partnerships, associations and groups of entities would fall within this description.

Composition of a group reporting entity

Section 2 of the DP considers how to circumscribe the area of business activity of interest to equity investors, lenders and other capital providers in the context of a group of entities.

The Boards’ preliminary view is that the composition of a group reporting entity should be based on control. The DP proposes that the composition of a group reporting entity should primarily be determined using the ‘controlling entity’ model, under which a group reporting entity comprises the controlling entity (the parent) and other entities under its control (i.e. its subsidiaries).

The DP also allows that there are some limited circumstances where the ‘common control’ model could be used to justify the preparation of ‘combined’ financial statements for two or more commonly-controlled entities. Such circumstances could exist, for example, if a lender has provided funding to several corporations controlled by an individual investor.

Preparation of consolidated financial statements

In keeping with the objective of providing useful information, the Boards propose that a parent entity should present consolidated financial statements. An entity would not be prevented from presenting parent-only financial statements provided they are included in the same report as the consolidated financial statements.

The Boards have also concluded that consolidated financial statements should be presented from the perspective of the group reporting entity (the 'entity' approach), not from the perspective of the parent entity's shareholders (the 'proprietary' approach).

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