



The South African Institute of Chartered Accountants

25 May 2007

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

Website: [www.iasb.org](http://www.iasb.org)

Dear Sir/Madam

***EXPOSURE DRAFT ON AMENDMENTS TO IAS 24 – RELATED PARTY DISCLOSURES: STATE-CONTROLLED ENTITIES AND THE DEFINITION OF A RELATED PARTY***

In response to your request for comments on the exposure draft on *Amendments to IAS 24 – Related Party Disclosures: State-controlled Entities and the Definition of a Related Party*, attached please find the comment letter prepared by the South African Institute of Chartered Accountants (SAICA). Please note that SAICA is not only a professional body, but is also secretariat for the Accounting Practices Board (APB), the official accounting standard setting body in South Africa.

This comment letter arises out of debates with SAICA's Accounting Practices Committee (the technical advisory body to the APB), a few listed private sector entities and public sector entities, all of whom would be classified as influenced by the state in terms of these proposed amendments.

We thank you for the opportunity to provide comments on this document. We have, in addition to our responses to the questions raised, also included general comments on aspects not specifically dealt with in the questions.

Please do not hesitate to contact us should you wish to discuss any of our comments.

Yours sincerely

**Sue Ludolph**  
**Project Director – Accounting**

cc: Moses Kgosana (Chairman of the Accounting Practices Board)  
Prof Alex Watson (Chairperson of the Accounting Practices Committee)



## ***RELATED PARTY DISCLOSURES***

### **GENERAL COMMENTS**

In principle, we welcome the Board's proposed amendments to IAS 24 – *Related Party Disclosures*, to provide an exemption from disclosure of related party transactions between state-controlled entities and to clarify the definition of a related party.

Although we generally support the direction of these proposed amendments, we have some concerns. Our most significant reservations about the proposed amendments are:

- The exemption, as noted in Question 1, should be extended to entities transacting with the state and not be limited to transactions between two state controlled, jointly controlled or significantly influenced entities.
- It would be appropriate to also exempt disclosure requirements from non-state entities that are under common control, where it is clear that there is no influence.
- The use of undefined terms “*significant voting power*”, “*influence*” and “*economically significant*”.
- Paragraph 17A(a) only refers to control and significant influence. We believe that it should also refer to joint control.
- Paragraph 20 inserts (j) which refers to commitments in the future, which is more akin to a contingency and not a commitment, and has the potential to scope in all executory contracts.

### **SPECIFIC COMMENTS ON QUESTIONS RAISED**

#### **Question 1**

(a) *Do you agree with the proposal to provide, in the circumstances described in this exposure draft, an exemption for entities controlled or significantly influenced by the state?*

*If not, why? What would you propose instead and why?*

We agree with the objective of the proposed amendment to provide exemption for entities controlled, jointly controlled or significantly influenced by the state.

Consideration should be given to extending the exemption to entities transacting with the state and not limiting the exemption to transactions between two state controlled, jointly controlled or significantly influenced entities. Transactions between an entity that is controlled, significantly influenced or jointly controlled by the state, and the state are very often conducted on an arms-length basis and are not influenced in any way by the entity's relationship with the state. Where there is no preferential pricing or other advantage arising from the transaction with the state, the entity will often be unable to identify the transactions with the state and will therefore be unable to comply with the disclosure requirements. Where the transactions are taking place at non-market rates,

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disclosure would be required, as one of the indicators would apply. Although such entities should continue to disclose the existence of control by the state, where such control exists, it is submitted that they should not disclose transactions with the state unless there is an indicator which requires disclosure.

In order to accommodate the above proposal we propose the following additional exemption to be inserted after paragraph 17A:

### **Transactions between the state and the entity**

A reporting entity is exempt from the disclosure requirements of paragraph 17 if:

- the entity is a related party only because the reporting entity is controlled or significantly influenced by the state and the transaction is with that state; and
- there are no indicators that the state influenced the reporting entity in the undertaking of transactions between the reporting entity and the state.

We would encourage the Board to debate whether it would be appropriate to also exempt disclosure requirements from non-state entities that are under common control, where it is clear that there is no influence. If this approach were to be adopted, it would result in a standard that applied principles consistently.

We request that the Board defines the word “*influence*” as used in paragraph 17A(b). IAS 24 defines “*significant influence*”, but the proposed amendments now refer to “*influence*” and this appears to be a lower level of influence than significant influence.

We are concerned that the indicators provided in paragraph 17B and 17C appear to be very broad and would therefore result, in most instances, in state controlled entities not being exempt. This is also due to the fact that “*economically significant*” transactions are not defined.

In our view the wording in paragraph 17A(a) could be misinterpreted as implying that two entities that are significantly influenced by the state are related parties of each other. This should be clarified by a footnote to paragraph 17A(a).

We propose that paragraph 17A, in addition to (a) and (b), includes (c). We reproduce 17A below in full with our recommended wording for (c), for ease of reference. We have provided a suggested heading to 17A to differentiate these requirements from the additional paragraph after 17A, as recommended above.

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### **Transactions between entities that are both related parties of the state**

*“17A A reporting entity is exempt from the disclosure requirements of paragraph 17 in relation to an entity if:*

- (a) the entity is a related party only because the reporting entity is controlled or significantly influenced by a state and the other entity is controlled or significantly influenced by that state; and*
- (b) there are no indicators that the reporting entity influenced, or was influenced by, that entity.”*
- (c) there are no indicators that the state influenced the reporting entity or the other entity.*

Paragraph 17D states that *“A reporting entity might identify other factors or circumstances that suggest the reporting entity could influence, or be influenced by, the related party that would require the reporting entity to comply with the requirements in paragraph 17.”* This paragraph seems to refer to ‘the potential to influence’, whereas 17A(b) seems to refer to ‘actual exercise’. We are of the view that the wording in 17D should be drafted consistently with paragraph 17A(b).

### **Question 1 (continued)**

*(b) Do you agree:*

- (i) that an indicator approach is an appropriate method for identifying when the exemption should be provided for entities controlled or significantly influenced by the state; and*
- (ii) that the proposed indicators are appropriate?*

*If not, why? What would you propose instead and why?*

We agree with the approach of having indicators to assist preparers in determining whether the exemption applies. We are of the view that the current wording of paragraph 17B reads as a rule and these will be read as the only indicators. In addition, the wording in 17B is inconsistent with paragraph 17D and BC17 which make the point that the indicators of influence in paragraphs 17B and 17C are not exhaustive. We therefore suggest the following change to paragraph 17B – *“Indicators that the influence referred to in paragraph 17A(b) exists could be (are) when the related parties...”*.

We are concerned that the indicators provided in paragraph 17B and 17C are difficult to interpret, when read with paragraph 11(c)(iii) of the standard. Very often a state controlled entity is the supplier of electricity, water, telecommunications or other essential services to other state controlled, jointly controlled or significantly influenced entities. Would disclosure be required in such circumstances because the transactions are economically significant? The purchaser of the service is unable to conduct business without those services. Or would disclosure not be required because of paragraph 11(c)(iii)? If disclosure is required, it seems that the exemption may be useless to many state controlled or influenced entities.

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### **Question 2**

- (a) *The definition of a related party in IAS 24 does not include, for a subsidiary's individual or separate financial statements, an associate of the subsidiary's controlling investor. The Board has decided that it should be included, and thus proposes to amend the definition of a related party. The Board similarly proposes that when the investor is a person, entities that are either significantly influenced or controlled by that person are to be treated as related to each other. Do you agree with this proposed amendment?*

*If not, why? What would you propose instead and why?*

Yes, we agree with both proposed amendments.

- (b) *IAS 24 does not define associates of an entity as related parties. However, when a person has significant influence over an entity and a close member of the family of that person has significant influence over another entity, IAS 24 defines those two entities as related parties. The Board proposes to align the definition for both types of ownership by excluding from the definition of a related party an entity that is significantly influenced by a person and an entity that is significantly influenced by a close member of the family of that person. Do you agree with the proposed amendment?*

*If not, why? What would you propose instead and why?*

Yes, we agree with the objective to obtain consistency. However, we are concerned about the following issues that affect this proposal and suggest the Board needs to consider these:

- It is unclear whether the proposed amendment requires two entities which are both significantly influenced by the state to provide disclosure of transactions between them when influence exists. This is noted in our response to Question 1.
  - There appears to be an anomaly with respect to key management. For example, when A has significant influence over B and is a member of the key management of C, B and C will be related. However, when A has significant influence over both B and C, they are not related. When A is a member of key management of both B and C, they are not related. The distinction given to key management should be explained in the Basis for Conclusions.
- (c) *IAS 24 defines any entity over which a member of the key management personnel of the reporting entity has control, joint control or significant influence, or in which the member holds significant voting power, as related to the reporting entity. However, the converse is not true. Thus, when the entity that a person controls, jointly controls or significantly influences, or in which the person has significant voting power, is the reporting entity and that person is a member of the key management personnel of another entity, that other entity is not defined as related*

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*to the reporting entity. The Board proposes to remove this inconsistency by expanding the definition to encompass both situations. Do you agree with the proposed amendment?*

*If not, why? What would you propose instead and why?*

Yes, we agree.

*(d) Do you agree with the proposal to clarify the definition of a related party? Does the wording proposed capture the same set of related parties as IAS 24 at present (except for the amendments described in (a)–(c) above)? Do you agree that the proposed wording improves the definition of a related party?*

*If not, why? What would you propose instead and why?*

Yes, we agree that the proposed wording improves the definition of a related party. However, we are of the view that the Board needs to clarify the meaning of “*significant voting power*” (paragraph 9 (b)(vi)), used in the current text of IAS 24 and in a number of other standards, but is not a defined term in IFRSs. This may create inconsistencies and divergence in practice.

### **Question 3**

*Do you agree with the proposal to clarify the definition of a related party transaction? If not, why? What changes would you propose and why?*

Although we agree with the proposed clarification of the definition of a related party, we have a concern with the introduction of commitments in both paragraphs 17 and 20.

Paragraph 20 inserts (j) which states that “*transactions or commitments to do something if a particular event occurs or does not occur in the future.*” This wording is more akin to a contingency, not a commitment, and has the potential to scope in all executory contracts, which we do not believe is the Board’s intention and would not provide any benefit to users or investors. We therefore recommend that the Board refers to commitments at non-market related rates, or clarifies what it means in the Basis for Conclusions.

We also wish to point out that all the other examples of transaction provided in paragraph 20 refer to what the entity has done in the past, whereas (j) is worded to include future transactions, which is inconsistent and not, in our view, beneficial to users or investors.

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### **Question 4**

*Do you have any other comments on the proposals?*

#### **Definition of close members of the family of an individual**

These proposals require a couple of amendments to the definition of “*Close members of the family of an individual*”, one of which is the deletion of the word “*may*”. As a result, the rebuttable presumption, which exists in the current definition, that the individuals described in sub-sections (a) to (c) are close members of the family, will be changed into a rule. We therefore recommend the Board retain the word “*may*” in the definition.

#### **Subsequent amendment**

Due to the change of the definition of a related party in paragraph 9, paragraph 11(a) in the current IAS 24 should be amended to delete reference to sections (d) and (f) of the definition of a related party.

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