International Accounting Standards Board (IASB)
First Floor
30 Cannon Street
London, EC4M 6XH
United Kingdom

Brussels, 25 March 2009

Comment Letter on
IASB Exposure Draft ED 10 Consolidated Financial Statements

Dear Board Members,

The International Private Equity and Venture Capital Valuation Board (IPEV Board) appreciates and welcomes the opportunity to provide its views on the Exposure Draft ED 10 Consolidated Financial Statements.

The IPEV Board believes that reporting the fair value of individual investments to investors enhances the transparency towards this group of stakeholders[1]. The IPEV Board also shares the concerns expressed on several occasions by the private equity and venture capital industry[2] regarding the impact of IAS 27. The reasons for these concerns are the following:

- Investors in private equity and venture capital funds cannot accurately assess the performance of their investments with consolidated accounts;
- Stakeholders of the private equity and venture capital entities in charge of managing the private equity or venture capital funds cannot accurately assess the performance and risks of these entities[3].

Since the implementation of IAS 27 in January 2005, experience has shown that consolidated financial accounts produced according to the requirements of IAS 27 are of little use for investors in private equity and venture capital funds or in private equity and venture capital management companies. As a result, private equity and venture capital fund managers and investors in those funds opt for other GAAP than IFRS on the basis that the latter require the production of consolidated accounts while the former, notably the US GAAP, have opted for the production of non-consolidated accounts for investment companies. This evolution also proves that the costs embedded in the production of two sets of financial information (one consisting of consolidated accounts under IAS 27 and one based on the fair value of the investments) have appeared to be unjustified for both fund managers and investors in the funds.

[1] See IPEV Board press release of 20 November 2008, available at: http://www.privateequityvaluation.com/documents/IPEV_Committee_Statement_v3_181108.pdf
[2] For example, "Impact of consolidation on private equity and venture capital entities following the implementation of the improvements of IAS 27: the production of misleading accounts – Case Study", EVCA Position Statements (2003), downloadable at: http://www.evca.eu/publicandregulatoryaffairs/evcapositionstatementsandpapers.aspx?id=182
[3] For more details, see footnote 2.

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In light of the need for convergence of GAAP on a global basis in order to increase transparency, the Exposure Draft ED 10 could have been an opportunity to solve the issues introduced by IAS 27 by moving the IFRS closer to the US GAAP.

However, the IPEV Board believes that the current text does not solve the issues of consolidation for private equity and venture capital entities because:

- The notion of control presented in the Exposure Draft will result in the production of consolidated accounts for the funds themselves if they control underlying companies;

- Several points expressed in the Exposure Draft could result in disqualifying an entity as agent while the motivations for such disqualification relate directly to the contractual obligations imposed by the principals. More specifically, the IPEV Board would like to draw the attention of the IASB on the Appendix B Application guidance B8 which states:

  > "*A performance-related fee of an agent is often distinguishable from the returns of the investors for whom the agent is acting. For example, an investor in a fund will benefit from increases in the value of the fund and suffer from decreases in the value of the fund. In contrast, an agent might be paid a performance-related fee for a specified period and the agent is unlikely to be required to contribute to the fund (i.e. refund fees already received) if the value of the fund decreases*"

  The IPEV Board strongly disagrees with this paragraph as the usual contractual terms between agent and principals in the private equity asset class foresee claw-backs on performance fees whenever the return of the fund decreases below a certain contractually pre-defined hurdle rate. This aspect does not undermine the quality of the private equity firms as agent because fulfilling this clause is a prerequisite to win the mandate from principals.

- The IPEV Board also disagrees with the basis for conclusions BC 91 which states:

  > "*In some cases, the line between principal and agent is blurred. An agent may have a dual role. For example, a fund manager may act in a fiduciary capacity and have a direct investment in the fund it is managing*".

  In the private equity and venture capital industry, fund managers are required by their investors to invest along them in the funds in order to achieve a high level of alignment of interest between the agent and the principals. The return to the agents on such investments is usually conditional to a specific contractually pre-defined return to be achieved by the principals on their own investments.

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In conclusion, the mere fact of making a direct investment in the fund does not automatically confer a dual role to the agent and further consideration should be given to the contractual obligations of these investments.

The IPEV Board remains at the disposal of the IASB and other stakeholders for further discussion on the issues noted above.

Very truly yours,

The International Private Equity and Venture Capital Valuation Board

Prof. Herman Daems

Chairman of the IPEV Board

The International Private Equity and Venture Capital Valuation Guidelines

The International Private Equity and Venture Capital Valuation Guidelines (IPEV Guidelines) were launched in March 2005 to reflect the need for greater comparability across the industry and for consistency with IFRS and US GAAP accounting principles. Valuation guidelines are used by the private equity and venture capital industry for valuing private equity investments and provide a framework for fund managers and investors to monitor the value of existing investments. The IPEV Guidelines are based on the overall principle of 'fair value' in order to be consistent with IFRS and US GAAP.

The International Private Equity and Venture Capital Valuation Board (IPEV Board) reports and is accountable to a general assembly composed of all the endorsing associations to manage the evolution of the guidelines going forward. The IPEV Guidelines have been endorsed by 36 national and regional trade associations.

For more information: http://www.privateequityvaluation.com.

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