

Mr Michel Barnier
Commissioner Internal Market and Services
European Commission
200 Rue de la Loi
1049 Bruxelles

Weinheim, 01/07/13

Dear Commissioner Barnier,

GREEN PAPER “LONG-TERM FINANCING OF THE EUROPEAN ECONOMY”

We appreciate the opportunity to comment on the Commission’s Green Paper on long-term financing.

The Association for Participation in the Development of Accounting Regulations for Family-owned Entities (VMEBF) was founded in 2006 and consists of German companies with a strong family shareholder background. Beyond its members, the association represents a large part of family-owned large and medium-sized entities in Germany, often legally organised in the form of partnerships. The objective of the VMEBF association is to make the role of German family businesses as stakeholders in the development of international accounting more visible and to act as a constructive partner for the standard setters and other accounting-related institutions like the International Auditing and Assurance Standards Board (IAASB). We work closely together with the German standard setter GASC and the German Institute of Chartered Auditors (IDW) as well as other political institutions.

As our activities are primarily concentrating on accounting questions, we will just comment on the paragraphs of the Green Paper that address those questions.

The question on whether fair value accounting principles have led to short-termism in investor behavior is complex to answer. Before discussing that question, the general suitability of fair value information has to be evaluated. We believe that the question of **when to** use fair value measurement is inextricably linked with the question of **how to** determine fair value. Hence, the suitability of fair value measurement concepts widely depends on the use of fair value as a measurement basis in individual circumstances. From our point of view, fair value measurement can lead to decision-useful information for assets and liabilities which will most likely be realized in the near future and where there are observable prices in an active market. However, as

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especially the IASB with its International Financial Reporting Standards turns towards expanding fair value measurement to instruments/transactions of which the related cash in- or outflow lies in the distant future (e.g. pension obligations) and/or which are without observable prices in an active market, we are severely concerned about the usefulness of that kind of information for investors – regardless of whether they are short-term or long-term investors. This leads us to the conclusion that fair value information should only be used in rare circumstances, and only if there are observable prices in active markets. Especially industrial companies with a huge number of non-financial items in their financial statements without such observable prices should therefore not be required to determine and disclose exaggerated fair value information on those items.

Fair values of non-financial instruments are generally difficult to determine. Valuation of intangible and tangible assets as part of acquisition accounting (purchase price allocations) and impairment tests are usually costly. Many entities have to charge external consultants or auditors with those tasks. However, the results are rather subjective. Thus, we prefer goodwill being amortized over a limited useful life instead of an impairment only regime. This leads to a reduction of the number of intangibles being recognized in the course of purchase price allocations and would allow an adequately conservative determination of useful lives.

With this in mind, we would like to discuss the argument of short-termism being promoted by fair value information. To decide on whether to provide long-term financing, investors as well as creditors usually require information about profits/losses, cash flows and risk exposures. Therefore, we understand that long-term financiers usually do not focus on fair value information making their investment decisions. In particular family businesses and the German “Mittelstand” – meaning entities with a majority of long-term investors – even tend to avoid providing fair value information in their financial statements as far as possible. Even listed companies do not usually realize their enterprise value by exploiting the ups and downs of fair values of their non-current assets and liabilities. We are aware that especially capital market oriented entities are trying to satisfy the information needs of short term oriented users of their financial statements by providing considerable fair value information, but we doubt if the balance sheet is the appropriate vehicle to provide this kind of information.

With this in mind, we believe the rules on financial reporting should take into account both, the perspective of long-term financiers and short-term investors. Summarizing the arguments mentioned above, this could mean limiting fair value information to financial items with observable market prices or limiting the use of fair value to special industries like banking or insurance. Any other fair market value indication necessary for short term oriented investors may be reported in the notes to the financial statements.

Taking a look at IFRS accounting rules today, we believe that disclosure requirements (esp. on fair value) should be reduced for non-financial companies in order to help preparers and users of financial statements focus on relevant information instead of creating more information overload. Moreover, we believe that current mod-

els on **when to** use fair values (e.g. IFRS 9) and **how to** determine fair value (e.g. IFRS 13) are flawed. For example, there is massive criticism regarding the omission of the reliability exemption when finalizing Phase I of IFRS 9. As measuring equity instruments without observable market prices at fair value might lead to rather arbitrary and flawed measures for the individual instruments, the omission of that exemption is heavily criticised. In addition, many believe that the classification criteria as described in IFRS 9 might work well in a financial institutions environment but not in other sectors like the manufacturing industry. As related to IFRS 13, we believe that the exit price model as described in the standard can only lead to decision-useful information for a limited number of transactions. In this context, the exit price approach should be complemented by an entry price approach for certain transactions.

However, we believe that the short-termism in investor behavior cannot be solved by solely changing accounting rules.

Finally, we would like to comment on the question regarding increasing the integration of financial and non-financial information. Although we are aware of the general demand for transparency regarding non-financial information, especially on sustainability aspects, we believe that there should be no standardized requirements for disclosure of non-financial information. At the moment, a huge number of entities are providing such information on a voluntary basis. From our point of view, standardizing such disclosure requirements would not necessarily lead to an increase in transparency but rather downgrade the efforts of those entities as they could be perceived as another regulatory requirement expanding an entity's annual report and leading to an increase in administrative expense and auditor's remuneration.

Regarding the extent and content of disclosures we also would like to point to the current discussions about a disclosure framework currently undertaken by the IASB and other standard setters and institutions (EFRAG, UK FRC, GASB). In our opinion, the question of integrating non-financial information should be discussed in a cost-benefit-context bearing in mind the need and extent of mandatory disclosures for the general public.

Should you have any further questions, please do not hesitate to contact us.

Kind regards,

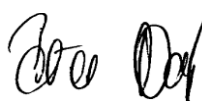
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