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5 August 2004

Sir David Tweedie
Chair of the International Accounting Standards Board
30 Cannon Street
London EC4M 6XH
United Kingdom

**RE: *Exposure Draft of Proposed Amendments to IFRS 3 “Business Combinations,”
Combinations by Contract Alone or Involving Mutual Entities***

Dear Sir David:

The Global Financial Reporting Advocacy Committee (GFRAC) of the CFA Institute¹ is pleased to respond to the International Accounting Standards Board (IASB) Exposure Draft (ED) of *Proposed Amendments to IFRS 3, “Business Combinations,” Combinations by Contract Alone or Involving Mutual Entities*. GFRAC is a standing committee of the CFA Institute charged with representing the views of investors to, and maintaining a liaison with, bodies that set financial reporting and disclosure standards in a global context, particularly the IASB. The committee is also charged with responding to requests for comment from national standard setters and regulators on international financial reporting issues. GFRAC includes CFA Institute members from Asia, Europe, and North America with varying professional backgrounds and expertise in the investment industry.

General Comments

The GFRAC strongly supports the requirement in IFRS 3 that all business combinations be accounted for by applying the purchase method. GFRAC commends the IASB for recognizing during its re-deliberations of IFRS 3 that the exclusion of combinations by contract alone or combinations involving mutual companies from the scope of IFRS 3 was inconsistent with the Board’s conclusion, as expressed in the basis of conclusions (BC) of IFRS 3, “that there are no circumstances in which the pooling of interests method provides information superior to that provided by the purchase method.” We strongly agree with this conclusion and the Board’s conclusion in this ED that combinations by contract alone and combinations involving mutual companies should be included within the scope of IFRS 3. Further, we would like to commend the IASB for rigorously applying its due process procedures by issuing this exposure draft for comment rather than simply amending the requirements of IFRS 3 before it was issued. We believe that due process is one of the most important elements of standard setting.

¹With headquarters in Charlottesville, VA and regional offices in Hong Kong and London, the CFA Institute [formerly, the Association for Investment Management and Research® (AIMR®)] is a non-profit professional association of more than 68,000 financial analysts, investment managers, and other investment professionals in 117 countries of which 57,000 are holders of the Chartered Financial Analyst® (CFA®) designation. The CFA Institute membership also includes 129 affiliated societies in 50 countries.

Question 1: Is this an appropriate interim solution to the accounting for such transactions until the Board develops guidance on applying the purchase method to such transactions as part of a subsequent phase of its Business Combinations project?

Yes, GFRAC believes that this is an acceptable interim solution. We concur with the Board's conclusion in paragraph BC8 of the Basis for Conclusions that "domestic legal, taxation or economic factors can sometimes make it difficult to identify an acquirer, [but] no exceptions to applying the purchase method should be permitted."

In fact, we do not think that the identification of an acquirer is necessary to applying purchase accounting for these transactions. GFRAC believes that in the circumstances where it is difficult to identify an acquirer it is preferable to revalue the assets and liabilities of all combining entities. In fact, GFRAC is a strong proponent of "fresh start" accounting. GFRAC hopes that this is a solution the IASB will explore in a subsequent phase of its business combinations project. The AIMR publication, *Financial Reporting in the 1990s and Beyond*, page 28 states the following:

[W]hen Firm A is purchased by Firm B, it is the assets and liabilities of Firm A that are recorded at their fair value, not those of Firm B. That is because those values are considered to have been validated by a transaction, even though the transaction was a single price for the entire firm and cannot be a reliable measure of the specific value of any of its components. One could then argue that whatever techniques are used to place values on the individual assets and liabilities of Firm A could be used to restate the assets and liabilities of Firm B. If not, then we perhaps ought not to apply them to Firm A.

Question 2: The Exposure Draft proposes that no amendments be made to the transitional and effective date requirements in IFRS 3. Is this appropriate?

Business combinations for which the agreement date is before 31 March 2004

The ED proposes that the transitional provisions of IFRS 3 should apply; that is, an entity is *permitted* to apply IFRS 3 from any date before 31 March 2004 *provided*:

1. the valuations and other information needed to apply that Standard to the past business combinations were obtained at the time those combinations were initially accounted for; and
2. the entity also applies IAS 36 and IAS 38 prospectively from that same date, and the valuations and other information needed to apply those Standards from that date were previously obtained so that there is no need to determine estimates that would need to have been made at a prior date.

That is, some entities may retroactively apply the requirements, while others will not

Once again GFRAC finds itself in the position of supporting the "lesser of two evils." We do not support the IFRS 3 transition for business combinations for which the agreement date is before 31 March 2004 even though we would normally support retrospective treatment. IFRS 3 permits but does not require retrospective treatment. We do not support alternatives in accounting standards. By permitting (in



certain circumstances) but not requiring retroactive application, this transition provision, in effect, provides an entity with alternatives.

Further, we would prefer a new accounting standard to be applied retrospectively so that all transactions in all periods are accounted for in a comparable manner. However, in the case of a new standard that requires information about values or judgments that may not have been obtained, made, or available at the date of the original transaction, we reluctantly agree that to require retroactive application would be begging for trouble. It would be requiring management to use information that may not exist or is no longer obtainable. The quality of the information produced would likely be unreliable. In such a situation, we believe that no entity should be permitted to retroactively apply the standard; i.e., retroactive application requiring previously unavailable data should be prohibited.

We recognize that it is unlikely that the IASB will amend IFRS 3 at this time to change the transition provision for business combinations that occurred prior to 31 March 2004. Therefore, GFRAC reluctantly supports the proposed transition for business combinations by contract or involving mutual entities. It sees no reason why the transition for these business combinations should differ from the transition provided any other business combination.

Business Combinations for which the agreement date is 31 March 2004 or later

The ED proposes that the transitional provisions of IFRS 3 should apply. That is, the provisions of this ED should be applied to business combinations for which the agreement date is 31 March 2004 or later.

GFRAC supports this transition. Since the IASB intends to finalize the ED expeditiously, but no later than the end of 2004, the period over which such transactions will not be covered by IFRS 3 will be relatively short. Therefore, our concerns about whether reliable and reasonably objective information will be available to restate such transactions (as expressed above) do not apply. The ED was issued nearly simultaneously with the issuance of IFRS 3, and companies potentially impacted by it are on notice that they must apply its provisions to all new transactions. Therefore, as they enter into new agreements, they should be thinking about the need to gather information and document the judgments that will need to be made when the ED is finalized.

Concluding Remarks

The GFRAC appreciates the opportunity to comment on this Exposure Draft. If you or the IASB staff have any questions or require further elaboration of our views, please do not hesitate to contact Patricia Doran Walters, CFA, at 1.434.951.5315 or patricia.walters@cfainstitute.org.

Sincerely,

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