CL 31

JPC/CA/nd/22.7/8/1 2 April 2003

Sir David Tweedie
Chairman
IASB
30 Cannon Street
GB-London EC4M 6XH

Dear Sir David,

RE: <u>BUSINESS COMBINATIONS</u>

UNICE is the umbrella organisation representing 34 central industrial and employers' federations from 27 European countries, speaking for more than 16 million companies.

UNICE would like to take this opportunity to offer the following comments on the IASB Business Combinations and Amendments to IAS 36 & 38 exposure drafts.

UNICE welcomes the convergence effort that has been conducted by the IASB in accounting for Business Combinations and Intangibles. In our view, convergence remains, on this issue as on others, a major concern.

However, the issues detailed below are raising concern among UNICE members.

1- Issues of the utmost importance

- **the cost of acquisition should be retained** as the best measurement of the net assets acquired:
  - ✓ management should remain accountable for the total investment decided and carried out,
  - ✓ the cost of acquisition should include the restructuring costs incurred in the business combination as planned at inception; we therefore recommend that a restructuring liability be recognised as part of the cost of acquisition, if conditions set in IAS 37 are met before the end of the allocation period and if the restructuring costs result without any possible doubt from the reduction of the acquiree's activities and the business combination,
  - ✓ goodwill is not measured on the grounds that have led to its recognition as an asset (that is the synergies involved in the business combination) if the cost of acquisition does not include all costs incurred, of all natures, directly attributable to the combination.

- **management's intent should be reflected**:
  - ✓ assets should be fair valued on the basis of management's intent (continuing or ceasing operations).

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- goodwill should not be allocated to the lowest level of cash generating unit at which management monitors return on investment. For the sake of comparability, greater consistency over time and convergence with US requirements, and also because it is consistent with the business logic, we recommend that **goodwill be allocated to the level of the segment or to the reporting unit one level below**.

- the proposed impairment test should be rejected as flawed. In applying the proposed impairment test, goodwill may have to be impaired because of a gain in value of one asset belonging to the cash generating unit to which it has been allocated, although that gain in value would never be recognised, if the asset was still to be carried at historical cost. There is no attempt to value goodwill appropriately, on the grounds that have led to its recognition as an asset. Furthermore, determining the implied value of goodwill as defined would be both costly and burdensome.
  In our view, **the present impairment test required in IAS 36 is rigorous enough** to ensure that no cash-generating unit is presented in the balance sheet in excess of its recoverable value. There is no need to introduce more complexity that would deny the economic interdependency of all assets included in cash-generating units or conflict with the mix-model measurement on which IFRS are currently built. Furthermore the suggestion that there should be greater efforts made to segregate internally generated and acquired goodwill seems thoroughly impractical.
  We also believe that requiring an impairment test to be carried out systematically at least once a year adequately strengthens the accounting for goodwill when switching from amortisation to impairment testing.
  Furthermore, we want to stress that the proposed screening mechanism is of the utmost importance to us, as it prevents entities from unnecessary burden.

- disclosures requested in the IASB proposal are far too excessive. Disclosures should be limited to the requirements included in FAS 142.

2- Issues that raise concern

- designating an acquirer arbitrarily in the very rare circumstances when there is none is not an improvement; we agree to the elimination of the pooling of interest method, but not until it is replaced by a more appropriate method; sound criteria and definitions should be set up, in order to avoid abuse.

- we agree that any minority interest in the acquiree be stated at the minority's proportion of the net fair values of the identifiable assets and liabilities. However this would result in a divergence from US requirements and deny European companies with the level playing field that they are seeking.

- In our view, contingent liabilities should not be recognised as part of the cost of acquisition, unless they meet IAS 37 criteria during the allocation period. Also, convergence with US GAAPs should be sought in accounting for guarantees.

- we do not support the option impairment or amortisation; however we support impairment only if we can rely on a robust, simple and cost-effective impairment test. Moreover we agree that amortisation should be regarded as more appropriate for small and medium entities. However we believe that the issue should be dealt with as part of the SME project that is currently in the research phase.

- impairment testing of intangible assets with indefinite useful life and goodwill should be carried out systematically as part of one single procedure, at the same time, and following the business planning cycle of the entity. Of course, within that single procedure, assets have to be tested for impairment first.

- we do not believe that management past ability of reliable forecasting should be reflected in the assumptions retained in measuring value in use. Management may have in the past gone through periods when forecast compared to real figures never show any specific pattern. Most of the time also there are quite sound reasons identified to justify the discrepancies. Such a proposal would infringe the requirement to base cash flow projections on most recent forecasts established by management, which, in our opinion, is an essential feature of sound impairment testing. Forecast updates are under review by the entity's external auditors and therefore no additional disclosure should be required.

- Management should have the option to prepare forecasts on a pre-tax or a post-tax basis.

- In our view, intangible assets with indefinite useful life and goodwill should be dealt with in the same way, in order to avoid any arbitrage between identifiable intangible asset and goodwill at the time the cost of acquisition is allocated. Therefore we recommend that impairment loss reversal be prohibited, for both intangible assets and goodwill.

The issues raised above are supported by all our members, provided that convergence is reached with present or future US GAAP requirements. We therefore recommend that convergence is sought and reached on the basis of the above. Some of our members have additional issues to raise, some of which being sensitive in specific industrial sectors, that they may address separately.

We remain at your full disposal to discuss this matter further.

Yours sincerely,

On behalf of
Jérôme P. Chauvin
Director, Company Affairs Department