acteo Association pour la participation des entreprises françaises à l'harmonisation comptable internationale

Mouvement des Entreprises de France
MEDEF

CL 77

➢ ED 3 BUSINESS COMBINATIONS

➢ ED AMENDMENTS TO :
- IAS 36 - Impairment of Assets
- IAS 38 – Intangible Assets

Question 1 : SCOPE

Acteo & Medef welcome the convergence effort that has been conducted by the IASB in accounting for Business Combinations and Intangibles.

However, the issues detailed below are raising concern among 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 recognized 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 doubt possible from the reduction of the acquiree' s activities and the business combination,
  - ✓ goodwill is not measured on the grounds that have lead to recognize it 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).

- goodwill should not be allocated to the lowest level of cash generating unit at which management monitors return on investment. In our view, one important feature in the allocation of goodwill is consistency over time. The lower goodwill is allocated, the less consistent will the allocation be over time, since allocating goodwill then becomes extremely sensitive to any change in the reporting structure. Also, for the sake of comparability, the level to which goodwill is allocated should not depend on the organisation choices made by management.
  More importantly, we believe that the most useful information is provided to users when aggregating cash generating units that constitute businesses with similar characteristics, notwithstanding the fact that they may be monitored, as far as internal reporting review is concerned, independently. We indeed believe that similar economic characteristics ensure a similar economic behaviour, excluding hence any opportunity for gains in value of a cash generating unit to offset losses of another.
  Since the right level to which goodwill should be allocated might be, in most cases, in line with US Gaaps requirements, we recommend an approach similar to present US Gaaps, that is **an allocation of goodwill at a level no lower than the first level below segment**. This will serve convergence and greater comparability from one entity to the other.

- 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 recognized, if the asset was still to be carried at historical cost. There is no attempt to value goodwill appropriately, on the grounds that have lead to recognise it as an

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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 amortization to impairment testing.

- Management forecasts always and naturally reflect the investments, restructuring, optimisation decisions that management intends to make in order to improve the entity's performance. Therefore the requirements of both present IAS 36 and the exposure draft should be reviewed in order to match the business logic. It is not sensible indeed to expect entities to build up theoretical cash flows forecasts designed for the sole purpose of supporting impairment testing. Entities would incur undue costs and effort and no reliability could be expected in forecasts that management would never either assess or approve. Moreover analysis of actual vs forecasted performance would be denied.

  We therefore suggest that the **requirement to base value in use on the most recent forecasts approved by management be retained, just as they are.**

  The value in use obtained for the CGU would still be comparable to its carrying value since all outflows resulting from the investment or restructuring to be conducted would be included in the projection.

- **Disclosures required are far too detailed** to be of any use to the reader of financial statements. A lot of data are requested, where qualitative and synthetic narratives would be far more useful to the understanding of the user of financial statements.

2- Issues that raise concern

- designating an acquirer arbitrarily in the very rare circumstances when there is none is not an improvement; the pooling of interest method should not be eliminated before a more adequate method is identified; sound criteria and definition need however 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.

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- Negative goodwill arising from future losses should not be recognised in profit and loss immediately, but should match the future losses when they occur. It is in our view appropriate to deal with positive and negative goodwill symmetrically and hence regard negative goodwill as “future outflows arising from the past business combination”.

- impairment testing of intangible assets with indefinite useful life and goodwill should be carried out systematically as part of one single procedure, simultaneously, and following the business planning cycle of the entity.

- we do not believe that management past ability of reliable forecasting should be reflected in the assumptions retained in measuring value in use. This would infringe the requirement to base cash flow projections on most recent forecasts established by management. Moreover 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. However we acknowledge that management past ability of reliable forecasting is an information useful to users. Therefore we recommend that an analysis by management should be disclosed, as to how and why last projections were under- or over- met.

Question 1 : SCOPE

QUESTIONS

Question 1 : SCOPE

The Exposure Draft proposes :

a) to exclude from the scope of the IFRS business combinations in which separate entities or operations of entities are brought together to form a joint venture, and business combinations involving entities under common control (see proposed paragraphs 2 and 3 and paragraphs BC9-BC11 of the Basis for Conclusions).

Are these scope exclusions appropriate? If not, why not ?

These scope exclusions do not constitute any change from the actual IAS 22. When encountering joint ventures and entities under common control, preparers and auditors are left with no standard whatsoever as to how to deal with these situations. In our opinion, such a situation is not adequate. It is however our understanding that these scope exclusions are not meant to survive Phase 2 of the Business Combinations project and we encourage the Board to undertake the necessary analysis in order to define the appropriate accounting treatment. We would oppose to phase 2, were these scope exclusions to be maintained.

b) to include in the IFRS a definition of business combinations involving entities under common control, and additional guidance on identifying such transactions (see proposed paragraphs 9-12 and Appendix A, and paragraphs BC12-BC15 of the Basis for Conclusions).

Are the definition and additional guidance helpful in identifying transactions within the scope exclusion ? If not, what additional guidance would you suggest, and why ?

We welcome the additional guidance as truly helpful.

Question 1 : SCOPE

<u>Question 2</u> : METHOD OF ACCOUNTING FOR BUSINESS COMBINATIONS

The Exposure Draft proposes to eliminate the use of the pooling of interests method and require all business combinations within its scope to be accounted for by applying the purchase method (see proposed paragraphs 13-15 and paragraphs BC18-BC35 of the Basis for Conclusions).

Is this appropriate ? If not, why not ? If you believe the pooling of interests method should be applied to a particular class of transactions, what criteria should be used to distinguish those transactions from other business combinations, and why ?

We cannot concur with the Board decision to deal with true mergers as if there was an identifiable acquirer. We disagree with the Board on that respect:

- it is not because criteria not subject to abuse are difficult to define that specific situations should be ignored. In trying to prevent abuse, the Board's intention is to promote comparability of accounts. Comparability of accounts cannot be achieved when the acquirer is arbitrarily designated ; moreover, in that case, relevance is heavily impaired;
- the Board announces that phase 2 of the Business Combinations project is likely to provide with an analysis of the fresh start method as a proper method of accounting for true mergers. If this proves right, there will still be the need for adequate criteria, and we do not see any good reason why the necessary definition effort has been postponed;
- in the meanwhile we consider the pooling of interests method more appropriate to true mergers than the purchase method that does not adequately reflect the situation at stake.

We therefore recommend the Board:

- not to amend the present IAS 22 as to accounting for true mergers before phase 2 of the project is completed,
- to include a proper definition of true mergers, in order to prevent from further abuse.

Question 3 : REVERSE ACQUISITIONS

Under IAS 22 Business Combinations, a business combination is accounted for as a reverse acquisition when an entity (the legal parent) obtains ownership of the equity of another entity (the legal subsidiary) but, as part of the exchange transaction, issues enough voting equity as consideration for control of the combined entity to pass to the owners of the legal subsidiary. In such circumstances, the legal subsidiary is deemed to be the acquirer. The Exposure Draft :

a) ***proposes to modify the circumstances in which a business combination could be regarded as a reverse acquisition by clarifying that for all business combinations effected through an exchange of equity interests, the acquirer is the combining entity that has the power to govern the financial and operating policies of the other entity (or entities) so as to obtain benefits from its (or their) activities. As a result, a reverse acquisition occurs when the legal subsidiary has the power to govern the financial and operating policies of the legal parent so as to obtain benefits from its activities (see proposed paragraph 21 and paragraphs BC37-BC41 of the Basis for Conclusions).***

   Is this an appropriate description of the circumstances in which a business combination should be accounted for as a reverse acquisition ? If not, under what circumstances, if any, should a business combination be accounted for as a reverse acquisition ?

   We agree with the Board's decision and intent to ensure that business combinations be accounted for in accordance with their substance rather than with their legal form. However we do not support paragraph 21 wording.
   In our view, reverse acquisitions situations should be described as very exceptional circumstances and dealt with accordingly. In those very rare cases, the entity should be required to disclose and justify all the facts that are very strong indicators that the business combination should be dealt with as a reverse acquisition. Sentences such as "Commonly, the acquirer is the larger entity…" should be removed. Paragraphs 19 and 20 already include appropriate guidance and paragraph 21 should not infer that they should not be applied to reverse acquisitions.
   Paragraph 21 should read as follows:
   " However, all pertinent facts and circumstances shall be considered to determine which of the combining entities has the power to govern the financial and operating policies of the other entity (or entities) so as to obtain benefits from its (or their) activities. In some rare circumstances, the legal subsidiary may be the entity that obtains the power to govern the financial and operating policies of its legal parent. This is the case when, for example, a private operating entity arranges to have itself "acquired" by a non-operating or dormant public entity as a means of obtaining a stock exchange listing. In such circumstances, called reverse acquisitions, the purchase method should be applied, the legal subsidiary being the acquirer. Guidance on the accounting for reverse acquisitions is provided in paragraphs B1 – B14 of Appendix B."

Question 5 : PROVISIONS FOR TERMINATING OR REDUCING THE ACTIVITIES OF THE ACQUIREE

b) ***proposes additional guidance on the accounting for reverse acquisitions (see proposed paragraphs B1-B14 of Appendix B).***
Is this additional guidance appropriate ? If not, why not ? Should any additional guidance be included ? If so, what specific guidance should be added ?

The guidance provided is adequate.

<u>Question 4</u> : IDENTIFY THE ACQUIRER WHEN A NEW ENTITY IS FORMED TO EFFECT A BUSINESS COMBINATION

The Exposure Draft proposes that when a new entity is formed to issue equity instruments to effect a business combination, one of the combining entities that existed before the combination should be adjudged the acquirer on the evidence available (see proposed paragraph 22 and paragraphs BC42-BC46 of the Basis for Conclusions).

Is this appropriate ? If not, why not ?

Yes, we agree.

<u>Question 5</u> : PROVISIONS FOR TERMINATING OR REDUCING THE ACTIVITIES OF THE ACQUIREE

Under IAS 22, an acquirer must recognise as part of allocating the cost of a business combination a provision for terminating or reducing the activities of the acquiree (a 'restructuring provision') that was not a liability of the acquiree at the acquisition date, provided the acquirer has satisfied specified criteria. The Exposure Draft proposes that an acquirer should recognise a restructuring provision as part of allocating the cost of a business combination only when the acquiree has, at the acquisition date, an existing liability for restructuring recognised in accordance with IAS 37 Provisions, Contingent Liabilities and Contingent Assets (see proposed paragraph 40 and paragraphs BC55-BC66 of the Basis for Conclusions).

Is this appropriate ? If not, what criteria should an acquirer be required to satisfy to recognise a restructuring provision that was not a liability of the acquiree as part of allocating the cost of a combination, and why ?

No, we do not agree. The Board's attempt to exclude from the allocation of the cost of a business combination any element that is not an asset or a liability of the acquiree at the date of acquisition is not, in our view, the most relevant approach.

In our view, management should be accountable to the shareholders for large and strategic investments such as the purchase of existing businesses. We therefore think that accounting for the business combination should reflect the goodwill arising from the transaction as planned by management.

In that respect, we agree with paragraph BC 98 of the basis of conclusions where goodwill is defined as an asset and is intended, if every asset and liability is measured appropriately, to reflect the synergies arising from the business combination, that is from both entities brought together, not from the acquiree or the acquirer.
Furthermore, a business combination is a unique operation, and in our opinion, there is no better measurement of the fair value of the acquisition than the total consideration (cash and other assets, including costs to incur to bring both entities into one) planned by management to create the synergies that goodwill is intended to reflect.

Terminating or reducing the activities of the acquiree results, most of the time, from the business combination itself, and represents the cost to pay to provide for the synergies as planned by management.

To exclude the cost of terminating or reducing activities from the allocation of the cost of acquisition leads to inadequate measurements as described below:

- the costs of restructuring would be shown as part of the operating performance of the combined entity which they are not,
- goodwill would be underestimated. In some cases, goodwill could be lead to be negative. A profit would have to be reported, while costs would be differed until restructuring costs become a liability in accordance with IAS 37.

This, in our view, lead to distortions of both the income statement and the balance sheet.

However we agree with the Board that no liability should be reported that is not compliant with IAS 37.
Therefore, provided that the commercial and industrial strategies have been publicly outlined no later than at the date of acquisition, in order to raise expectations as to the future restructuring plan, we recommend that the cost of terminating or reducing the activities of the acquiree be included in the allocation of the cost of the acquisition. Those costs would be reported as liability as soon as the conditions set in IAS 37 are met; setting up a restructuring plan within twelve months of the acquisition date is feasible under European laws. We want to draw the Board's attention to the underlying reality in Europe where laying off employees cannot be decided and carried out as easily and rapidly as it is in the United States.

In order to avoid abuse, we recommend that the Board set up criteria to which the restructuring plan should be assessed, in order to make sure that the plan actually results from the combination of the two entities.

By extension of the above, and although the question is not raised as such, we recommend that assets acquired in the combination be accounted for at fair value, fair value being:

- the value in use, on the basis of the discounted cash flows planned by management past the combination, in those cases when the asset is to be maintained in operations,
- the net selling price (or fair value less costs to sell) of the asset, in those cases when the asset is to be disposed of.

To make management accountable for the business combination, the whole transaction should hence be reported reflecting management's intent. With the accompanying explanatory disclosures, we feel that information would be more useful to users than it would be according to the present draft.

<u>Question 5</u> : PROVISIONS FOR TERMINATING OR REDUCING THE ACTIVITIES OF THE ACQUIREE

Question 6 : CONTINGENT LIABILITIES

The Exposure Draft proposes that an acquirer should recognise separately the acquiree's contingent liabilities at the acquisition date as part of allocating the cost of a business combination, provided their fair values can be measured reliably (see proposed paragraphs 36 and 45 and paragraphs BC80-BC85 of the Basis for Conclusions).

Is this appropriate ? If not, why not ?

No, we do not agree.
Identifiable and measurable contingent liabilities may have influenced the total consideration that management agreed to in the acquisition.
However we believe that no liability should be recognised that does not meet IAS 37 definition and recognition criteria. Therefore contingent liabilities arising from an acquisition and of which fair value can be measured reliably should not be allocated as part of the cost of acquisition, unless they meet IAS 37 criteria before the end of the allocation period.

However we would like to stress that, in our view, circumstances are very rare when contingent liabilities are measured reliably at the time of acquisition without being subject to a liability guarantee.

Question 7 : MEASURING THE IDENTIFIABLE ASSETS ACQUIRED AND LIABILITIES AND CONTINGENT LIABILITIES ASSUMED

IAS 22 includes a benchmark and an allowed alternative treatment for the initial measurement of the identifiable net assets acquired in a business combination, and therefore for the initial measurement of any minority interests. The Exposure Draft proposes requiring the acquiree's identifiable assets, liabilities and contingent liabilities recognised as part of allocating the cost to be measured initially by the acquirer at their fair values at the acquisition date. Therefore, any minority interest in the acquiree will be stated at the minority's proportion of the net fair values of those items. This proposal is consistent with the allowed alternative treatment in IAS 22 (see proposed paragraphs 35 and 39 and paragraphs BC88-BC95 of the Basis for Conclusions).

Is this appropriate ? If not, how should the acquiree's identifiable assets, liabilities and contingent liabilities recognised as part of allocating the cost of a business combination be measured when there is a minority interest in the acquiree, and why ?

We agree that the elimination of the option and the treatment retained are appropriate. We however wish that convergence with US Gaaps be reached on that specific matter since it might affect comparability of performance among entities greatly.

Question 8 : GOODWILL

The Exposure Draft proposes that goodwill acquired in a business combination should be recognised as an asset and should not be amortised. Instead, it should be accounted for after initial recognition at cost less any accumulated impairment losses (see proposed paragraphs 50-54 and paragraphs BC96-BC108 of the Basis for Conclusions).

Do you agree that goodwill acquired in a business combination should be recognised as an asset ? If not, how should it be accounted for initially, and Why ? Should goodwill be accounted for after initial recognition at cost less any accumulated impairment losses ? If not, how should it be accounted for after initial recognition, and why ?

We agree with the proposals by the Board. We believe that impairment should drive entities to report more meaningful accounts that amortisation does. However to make that change for the better, entities need to be subject to strong, robust and easy to implement impairment tests.

Question 9 : EXCESS OVER THE COST OF A BUSINESS COMBINATION OF THE ACQUIRER'S INTEREST IN THE NET FAIR VALUE OF THE ACQUIREE'S IDENTIFIABLE ASSETS, LIABILITIES AND CONTINGENTS LIABILITIES

In some business combinations, the acquirer's interest in the net fair value of the acquiree's identifiable assets, liabilities and contingent liabilities recognised as part of allocating the cost of the combination exceeds that cost. The Exposure Draft proposes that when such an excess exists, the acquirer should :

a) reassess the identification and measurement of the acquiree's identifiable assets, liabilities and contingent liabilities and the measurement of the cost of the combination; and

b) recognise immediately in profit or loss any excess remaining after that reassessment.

(See proposed paragraphs 55 and 56 and paragraphs BC109-BC120 of the Basis for Conclusions.)

Is this treatment appropriate ? If not, how should any such excess be accounted for, and why ?

We disagree with the Board's proposal.
We believe that the same reasoning should apply, whether goodwill arises positive or negative.
In those circumstances when negative goodwill arises, and that future losses are known and planned, goodwill should be considered as "future outflows arising from past transactions" and hence be recognised as a liability.

Our recommendation is as follows:

- negative goodwill arising from accounting policies not requiring accounting for assets and liabilities at fair value, or from a true bargain should be recognised in profit and loss immediately;
- negative goodwill arising from future losses, planned restructuring and contingent liabilities should match those losses in profit and loss in the period when they are incurred.

The entity should regularly test that negative goodwill need to be maintained.

Question 10 : COMPLETING THE INTIAL ACCOUNTING FOR A BUSINESS COMBINATION AND SUBSEQUENT ADJUSTMENTS TO THAT ACCOUNTING

The Exposure Draft proposes that :

a) if the initial accounting for a business combination can be determined only provisionally by the end of the reporting period in which the combination occurs because either the fair values to be assigned to the acquiree's identifiable assets, liabilities or contingent liabilities or the cost of the combination can be determined only provisionally, the acquirer should account for the combination using those provisional values. Any adjustment to those values as a result of completing the initial accounting is to be recognised within twelve months of the acquisition date (see proposed paragraphs 60 and 61 and paragraphs BC123-BC126 of the Basis for Conclusions).

Is twelve months from the acquisition date sufficient time for completing the accounting for a business combination ? If not, what period would be sufficient, and why ?

Twelve months from the acquisition is sufficient time for completing the accounting for a business combination.

b) with some exceptions carried forward as an interim measure from IAS 22, adjustments to the initial accounting for a business combination after that accounting is complete should be recognised only to correct an error (see proposed paragraphs 62 and 63 and paragraphs BC127-BC132 of the Basis for Conclusions).

Is this appropriate ? If not, under what other circumstances should the initial accounting be amended after it is complete, and why?

We agree with the present draft requirements.

AMENDMENTS TO IAS 36

Question 1 : FREQUENCY OF IMPAIRMENT TESTS

Are the proposals relating to the frequency of impairment testing intangible assets with indefinite useful lives and acquired goodwill appropriate (see proposed paragraphs 8 and 8A and paragraphs C6, C7 and C41 of the Basis for Conclusions) ? If not, how often should such assets be tested for impairment, and why ?

We believe it is reasonable to carry out an annual impairment test of intangible assets with indefinite useful lives and acquired goodwill. However we recommend that the Board adjust slightly their proposals***:***

- to set up the same frequency for both intangible assets with indefinite useful lives and acquired goodwill: the impairment tests should be carried out simultaneously;
- to leave to the entity the choice of when those tests should be carried out during the year; it indeed seems right to have the impairment testing procedures match the budget setting procedures, which may vary in timing from one company to the next.

Evidently an impairment test should be carried out every time there is an indication that an asset might be impaired, whenever the indication arises.

Question 2 : INTANGIBLE ASSETS WITH INDEFINITE USEFUL LIVES

The Exposure Draft proposes that the recoverable amount of an intangible asset with an indefinite useful life should be measured, and impairment losses (and reversals of impairment losses) for such assets accounted for, in accordance with the requirements in IAS 36 for assets other than goodwill (see paragraphs C10-C11 of the Basis for Conclusions).
Is this appropriate? If not, how should the recoverable amount be measured, and impairment losses (and reversals of impairment losses) be accounted for?

We agree with the Board's proposals.

Question 3 : MEASURING VALUE IN USE

The Exposure Draft proposes additional guidance on measuring the value in use of an asset. Is this additional guidance appropriate ?
In particular :

(a) should an asset's value in use reflect the elements listed in proposed paragraph 25A ? If not, which elements should be excluded or should any additional elements be included ? Also, should an entity be permitted to reflect those elements either as adjustments to the future cash flows or adjustments to the discount rate (see proposed paragraph 26A and paragraphs C66 and C67 of the Basis for Conclusions) ? If not, which approach should be required ?

The exposure draft is consistent with present IAS 36 in requiring that:

- value in use be based on the most recent forecasts approved by management, and
- any investment increasing performance or capacity of the assets under review or restructuring cost be excluded of the forecasts.

In practice these two requirements are conflicting with each other. Management forecasts always and naturally reflect the investments, restructuring, optimisation decisions that management intends to make in order to improve the entity's performance. Therefore the requirements of both present IAS 36 and the exposure draft should be reviewed in order to match the business logic. It is not sensible indeed to expect entities to build up theoretical cash flows forecasts designed for the sole purpose of supporting impairment testing. Entities would incur undue costs and effort and no reliability could be expected in forecasts that management would never either assess or approve. Moreover analysis of actual vs forecasted performance would be denied.
We therefore suggest that the requirement to base value in use on the most recent forecasts approved by management be retained, just as they are.
The value in use obtained for the CGU would still be comparable to its carrying value since all outflows resulting from the investment or restructuring to be conducted would be included in the projection.

Aside that first comment, we believe that paragraph 25A describes appropriately how an asset's value in use should be determined. We believe that an entity should be permitted to reflect those elements either as adjustments to the future cash flows or as adjustments to the discount rate.
Some entities are favourable to having the choice to carry those projections after tax; such a choice is open under US Gaaps. Those entities have set up monitoring procedures, measuring performance as financial investors do, that is after tax.

(b) should the assumptions on which cash flow projections are based take into account both past actual cash flows and management's past ability to forecast cash flows accurately (see proposed paragraph 27(a)(ii) and paragraphs C66 and C67 of the Basis for Conclusions) ? If not, why not ?

Considering management's past ability to forecast cash flows accurately in determining what assumptions should be retained as a basis for cash flow projections seems at first sight appealing.
However it is not, in our view, appropriate and consistent with the standard's requirements.

One main feature of impairment testing is to base cash flow projections on most recent forecasts established by management. There is not one entity in which forecasts are carried out by management, that management would adjust to reflect past discrepancies between forecast and realised figures.

Moreover, management may have in the past gone through periods when forecast compared to real figures never show any specific pattern. Most of the time there are quite sound reasons identified to justify the discrepancies (September 11th in the Aeronautics, a new competitor or an old one that has gone out of the market….), all justifications that management is able to identify when comparing actual and forecast performances. When would such a justification be retained as being sound, when should it be rejected and last forecasts be adjusted?

The standard also requires that an impairment test be carried out immediately whenever there is an indication that an asset or cash generating unit might be impaired. One strong internal indicator for such an impairment test to be carried out is that forecast performance is not met.

For all the reasons above, we believe the information most relevant and useful to users would be:
- to retain management's last forecasts as basis for impairment testing,
- to require that an analysis by management be disclosed, as to how and why last projections were under- or over- met.

Question 4 : ALLOCATING GOODWILL TO CASH-GENERATING UNITS

The Exposure Draft proposes that for the purpose of impairment testing, acquired goodwill should be allocated to one or more cash-generating units.

(a) Should the allocation of goodwill to one or more cash-generating units result in the goodwill being tested for impairment at a level that is consistent with the lowest level at which management monitors the return on the investment in that goodwill, provided such monitoring is conducted at or below the segment level based on an entity's primary reporting format (see proposed paragraphs 73-77 and paragraphs C18- C20 of the Basis for Conclusions)? If not, at what level should the goodwill be tested for impairment, and why ?

In our view, one important feature in the allocation of goodwill is consistency over time. The lower goodwill is allocated, the less consistent will the allocation be over time, since allocating goodwill then becomes extremely sensitive to any change in the reporting structure.
Moreover we believe that the most useful information is provided to users when aggregating cash generating units that constitute businesses with similar characteristics, notwithstanding the fact that they may be monitored, as far as internal reporting review is concerned, independently. We indeed believe that similar economic characteristics ensure a similar economic behaviour, excluding hence any opportunity for gains in value of a cash generating unit to offset losses of another.
Therefore we recommend an approach similar to present US Gaaps, that is an allocation of goodwill at a level no lower than the first level below segment.

(b) If an entity disposes of an operation within a cash-generating unit to which goodwill has been allocated, should the goodwill associated with that operation be included in the carrying amount of the operation when determining the gain or loss on disposal (see proposed paragraph 81 and paragraphs C21-C23 of the Basis for Conclusions) ? If not, why not ? If so, should the amount of the goodwill be measured on the basis of the relative values of the operation disposed of and the portion of the unit retained or on some other basis ?

We agree with the proposal. Whenever goodwill has been allocated at a level higher than the cash generating unit being disposed of, we recommend that goodwill associated with the disposal operation be measured on the basis of the relative discounted cash flows of all cash generating units to which goodwill was allocated globally.

(c) If an entity reorganises its reporting structure in a manner that changes the composition of one or more cash-generating units to which goodwill has been allocated, should the goodwill be reallocated to the units affected using a relative value approach (see proposed paragraph 82 and paragraphs C24 and C25 of the Basis for Conclusions) ? If not, what approach should be used ?

We agree that goodwill be re-allocated and we agree with the proposed approach. We however believe that the less it happens, the more relevant and useful the information provided, and favour the greatest consistency over time, as explained in our answer to question a) above.

Question 5 : DETERMINING WHETHER GOODWILL IS IMPAIRED

The Exposure Draft proposes :

(a) that the recoverable amount of a cash-generating unit to which goodwill has been allocated should be measured as the higher of the unit's value in use and net selling price (see proposed paragraphs 5 (definition of recoverable amount) and 85 and paragraph C17 of the Basis for Conclusions).
Is this appropriate? If not, how should the recoverable amount of the unit be measured ?

We agree with the basis for conclusions.

(b) the use of a screening mechanism for identifying potential goodwill impairments, whereby goodwill allocated to a cash-generating unit would be identified as potentially impaired only when the carrying amount of the unit exceeds its recoverable amount (see proposed paragraph 85 and paragraphs C42-C51 of the Basis for Conclusions).
Is this an appropriate method for identifying potential goodwill impairments ? If not, what other method should be used ?

We believe that the impairment test as defined in present IAS 36 should be maintained.

(c) that if an entity identifies goodwill allocated to a cash-generating unit as potentially impaired, the amount of any impairment loss for that goodwill should be measured as the excess of the goodwill's carrying amount over its implied value measured in accordance with proposed paragraph 86 (see proposed paragraphs 85 and 86 and paragraphs C28-C40 of the Basis for Conclusions).
Is this an appropriate method for measuring impairment losses for goodwill ? If not, what method should be used, and why ?

We believe 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 recognized, if the asset was still to be carried at historical cost. There is no attempt to value goodwill appropriately, on the grounds that have lead to recognise it 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 amortization to impairment testing.

Question 6 : REVERSALS OF IMPAIRMENT LOSSES FOR GOODWILL

The Exposure Draft proposes that reversals of impairment losses recognised for goodwill should be prohibited (see proposed paragraph 123 and paragraphs C62-C65 of the Basis for Conclusions).
Is this appropriate ? If not, what are the circumstances in which reversals of impairment losses for goodwill should be recognised ?

We agree with the Board's proposal. However we believe that the exception included in present IAS 36 should be maintained. Impairment losses for goodwill should be recognised, if and only if the exact events that triggered the impairment do reverse.

Question 7 : ESTIMATES USED TO MEASURE RECOVERABLE AMOUNTS OF CASH GENERATING UNITS CONTAINING GOODWILL OR INTANGIBLE ASSETS WITH INDEFINITE USEFUL LIVES

The Exposure Draft proposes requiring a variety of information to be disclosed for each segment, based on an entity's primary reporting format, that includes within its carrying amount goodwill or intangible assets with indefinite useful lives (see proposed paragraph 134 and paragraphs C69-C82 of the Basis for Conclusions).

(a) ***Should an entity be required to disclose each of the items in proposed paragraph 134 ? If not, which items should be removed from the disclosure requirements, and why ?***

(b) ***Should the information to be disclosed under proposed paragraph 134 be disclosed separately for a cash-generating unit within a segment when one or more of the criteria in proposed paragraph 137 are satisfied ? If not, why not ?***

We do not believe that the list of information to be disclosed as displayed in § 134 and § 137 would serve the user of financial statements right. However we agree that all information necessary for a good understanding of the analysis and assumptions made in the business is required.

Therefore management should include a narrative including those quantitative data as deemed necessary in the circumstances and explaining the assumptions underlying the cash flow forecasts on which value in use are based.
Users should hence be entitled to understand the conclusions that were reached on the basis of management analysis instead of being invited to review every single parameter included in the forecasts. Moreover some of the parameters listed by the Board (% market shares, %gross margins…) are confidential data that should not be made public.

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AMENDMENTS TO IAS 38

Question 1 : IDENTIFIABILITY

The Exposure Draft proposes that an asset should be treated as meeting the identifiability criterion in the definition of an intangible asset when it is separable or arises from contractual or other legal rights (see proposed paragraphs 10 and 11 and paragraphs B6-B10 of the Basis for Conclusions).

Are the separability and contractual/other legal rights criteria appropriate for determining whether an asset meets the identifiability criterion in the definition of an intangible asset ? If not, what criteria are appropriate, and why ?

Yes, we agree.

Question 2 : CRITERIA FOR RECOGNISING INTANGIBLE ASSETS ACQUIRED IN A BUSINESS COMBINATION SEPARATELY FROM GOODWILL

This Exposure Draft proposes clarifying that for an intangible asset acquired in a business combination, the probability recognition criterion will always be satisfied and, with the exception of an assembled workforce, sufficient information should always exist to measure its fair value reliably (see proposed paragraphs 29-32 and paragraphs B11-B15 of the Basis for Conclusions). Therefore, as proposed in ED 3, an Exposure Draft of a proposed International Financial Reporting Standard Business Combinations, an acquirer should recognise, at the acquisition date and separately from goodwill, all of the acquiree's intangible assets, excluding an assembled workforce, that meet the definition of an intangible asset (see proposed paragraphs 36, 43 and 44 of ED 3).

Do you agree that, with the exception of an assembled workforce, sufficient information can reasonably be expected to exist to measure reliably the fair value of an intangible asset acquired in a business combination ? If not, why not ? The Board would appreciate respondents outlining the specific circumstances in which the fair value of an intangible asset acquired in a business combination could not be measured reliably.

Measurability of intangible assets has always been a difficult issue. Therefore we do not agree with the Board on this issue, since we do not believe it is reasonable to assume that all identifiable intangible assets will –with the exception of a work-force- be measurable in all situations arising in business combinations.
Also we recommend that intangible assets acquired in the combination be accounted for at fair value, fair value being:

- the value in use, on the basis of the discounted cash flows planned by management past the combination, in those cases when the asset is to be maintained in operations,

Question 10 : COMPLETING THE INTIAL ACCOUNTING FOR A BUSINESS COMBINATION AND SUBSEQUENT ADJUSTMENTS TO THAT ACCOUNTING

- the net selling price (or fair value less costs to sell) of the asset, in those cases when the asset is to be disposed of. Would the sale of the acquired assets fail during the allocation time of ***the*** cost of acquisition, the fair value of the assets acquired would have to be deemed equal to zero.

Question 3 : INDEFINITE USEFUL LIFE

The Exposure Draft proposes to remove from IAS 38 the rebuttable presumption that an intangible asset's useful life cannot exceed twenty years, and to require its useful life to be regarded as indefinite when, based on an analysis of all of the relevant factors, there is no foreseeable limit on the period of time over which the asset is expected to generate net cash inflows for the entity (see proposed paragraphs 85-88 and paragraphs B29-B32 of the Basis for Conclusions).

Is this appropriate ? If not, under what circumstances, if any, should an intangible asset be regarded as having an indefinite useful life ?

Yes we believe it is appropriate.

Question 4 : USEFUL LIFE OF INTANGIBLE ASSET ARISING FROM CONTRACTUAL OR OTHER LEGAL RIGHTS

The Exposure Draft proposes that if an intangible asset arises from contractual or other legal rights that are conveyed for a limited term that can be renewed, the useful life shall include the renewal period(s) only if there is evidence to support renewal by the entity without significant cost (see proposed paragraphs 91 and 92 and paragraphs B33-B35 of the Basis for Conclusions).

Is this an appropriate basis for determining the useful life of an intangible asset arising from contractual or other legal rights that are conveyed for a limited term that can be renewed ? If not, under what circumstances should the useful life include the renewal period(s) ?

Yes we believe it is appropriate.

Question 5 : NON-AMORTISATION OF INTANGIBLE ASSETS WITH INDEFINITE USEFUL LIVES

The Exposure Draft proposes that an intangible asset with an indefinite useful life should not be amortised (see proposed paragraphs 103 and 104 and paragraphs B36-B38 of the Basis for Conclusions).

Is this appropriate ? If not, how should such assets be accounted for after their initial recognition ?

Yes we believe it is appropriate.

Question 10 : COMPLETING THE INTIAL ACCOUNTING FOR A BUSINESS COMBINATION AND SUBSEQUENT ADJUSTMENTS TO THAT ACCOUNTING