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For the attention of Annette Kimmitt, Senior Project Manager

International Accounting Standards Board
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4 April 2003

Exposure draft ED3 Business Combinations and amendments to IAS36, Impairment of Assets, and IAS 38, Intangible Assets

Dear Sirs

In response to your invitation to comment, and as a preparer of accounts under International Financial Reporting Standards, I am pleased to attach our comments on the above mentioned exposure drafts.

Yours faithfully,

John Ramsay
Group Financial Controller
Syngenta AG

A. General Comments

The proposals would bring about, for business combinations only, a significant conceptual change in respect of contingent liabilities and intangible assets. It is undesirable to set up different criteria for the same elements in this manner, particularly as the transformation of probability from a criterion for recognition to a criterion for measurement is so fundamental that it would be quite wrong to introduce it through the back door without due process.

While on balance we see the merits of an impairment-only approach to subsequent measurement of goodwill and indefinite-life intangibles, we believe that there is also a case for leaving the amortisation approach for goodwill in situations where a definite life can be estimated, analogous to other intangible assets.

The two-step impairment testing is potentially a very costly process, to be borne either by shareholders or by customers. We appreciate that the proposals do make some efforts to reduce the cost and effort involved through screening, but the simplification must go further if substantial costs are to be avoided, and we make some additional suggestions in this respect.

Convergence with US GAAP is a major concern, especially with regard to the level at which impairment testing is performed. It is not clear to us that the proposals in the ED of amendments to IAS 36 will permit impairment tests to be performed at the same level as the similar impairment testing under FAS 142, which potentially implies parallel IFRS and US GAAP calculations. We have suggested below how this could be resolved.

Disclosure requirements, particularly in revised IAS 36, are in our view excessive, particularly in comparison to FAS 142.

B. Answers to the IASB's Specific Questions on ED3

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?

(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?

Response

We agree with the Board's proposals.

Question 2 – 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?

Response

We believe that purchase accounting is the appropriate method for business combinations in which one of the combining entities obtains control of the other.

Paragraph BC27 of the basis for Conclusions to the ED leaves open the possibility of "true mergers". The Board states that further work is required to determine or confirm whether these exist and if so, what the appropriate accounting treatment for them is. In our view, if the previous uniting of interest treatment is prohibited now in favour of the purchase method, and this in its turn were to be replaced by "fresh start" accounting when a new IFRS emerges from the Business Combinations Phase II project, there could be problems in transitioning from the existing IAS 22 to the eventual confirmed treatment for "true mergers". In order to avoid such problems, it would be preferable:

- either to delay the mandatory application date of this draft IFRS (while still encouraging early application) until that further work has been completed; or
- to provide more specific interim guidance on how a "true merger" should be treated, particularly as regards how the deemed acquirer should be identified if the purchase method is to be applied to "true mergers" for an interim period.

To do neither of these might, in our view, result in one of the combining parties in a “true merger” being inappropriately identified as the acquirer, during the interim period between the application date of this draft IFRS and the date that a new IFRS emerges from the Business Combinations Phase II project.

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?

(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?

Response

(a) We agree with the proposed description of the circumstances in which a business combination should be accounted for as a reverse acquisition.

(b) The proposed additional guidance together with the illustrative examples is appropriate, but it would be helpful if the IFRS made it clear that the comparative figures presented should be those of the legal subsidiary and not those of the legal parent.

Question 4 – identifying an 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?

Response

We do agree with the proposal in cases where one of the existing entities can be identified as the acquirer, based on the criteria in paragraphs 17 to 21 of the ED. However, please see our reply to question 2 above. In our view, the Board should provide further guidance to assist in determining which entity is the acquirer, or the deemed acquirer, in borderline situations which may be "true mergers", if the purchase method is to be applied to those situations.

Question 5 – Provisions for terminating or reducing 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?

Response

We note the Board's conceptual arguments in favour of not recognizing such provisions in purchase accounting except where they are liabilities of the acquiree at the acquisition date under normal IAS 37 criteria.

Paragraph BC97 of the Basis for Conclusions to the ED observes that one element of core goodwill is the fair value of expected synergies from the combination. In our view, the value which the acquirer will place on this in practice, which will influence the cost of the business combination and the amount of goodwill, will be reduced by the present value of any restructuring costs which the acquirer foresees as necessary to incur in order to achieve the synergies. It could be argued that the present value at acquisition date of these restructuring costs will create a further cushion against goodwill impairment, in addition to any cushion which may arise from the acquirer's pre-combination internally generated goodwill (the latter as observed in paragraphs C37-40 of the Basis for Conclusions to the proposed revised IAS 36). This needs to be balanced against the perceived benefits of the proposed change.

In our view, this may represent an argument in favour of continuing with the existing treatment of restructuring costs in paragraph 31 of IAS 22 on pragmatic grounds. In our view, any scope which may currently be perceived to exist for potential abuse through purchase accounting of restructuring costs, is limited in practice, mainly by the strict criteria already incorporated into IAS 22, but also by the increased risk of future goodwill impairment which an entity would impose on itself if the initial amount of goodwill were inflated by restructuring provisions.

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?

Response

No, we do not believe that the proposal is appropriate because:

- In our view, it will not generally be possible to determine whether any identifiable reductions in the purchase price offered by the acquirer, which might provide the clearest evidence of the fair value of contingent liabilities at the acquisition date, relate solely to the acquirer's view of the fair value of any related contingent liabilities it is acquiring, or also to other reasons;

- It will lead to inconsistent accounting for contingent liabilities acquired in a business combination compared to other contingent liabilities, which will still be accounted for under IAS 37; and
- There will be many practical problems in arriving at a fair value of contingent liabilities subsequently which would be acceptable for audit purposes, in order to comply with paragraph 46 of the ED. For example, we believe that in most cases legal advisers would not be prepared to quantify a fair value for contingent liabilities arising from litigation or potential litigation, on grounds of caution. (In addition we must stress that disclosure of such values relating to litigation in process may be seriously prejudicial to the entity, especially where the link between amount and individual case is readily apparent).

Also, we believe that changing the recognition and measurement of contingent liabilities from the "non recognition until probable" approach of IAS 37 to a fair value approach, would represent a fundamental change to the conceptual framework, as it suggests to us that fair value is considered as the preferred measurement basis for the items in the financial statements. In our view, a separate Concepts project, rather than inclusion in ED3, would be the right way to propose the introduction of such a change.

For these reasons, we believe that contingent liabilities should continue not to be recognized unless a cash outflow becomes probable and they meet the definition of a liability, in accordance with IAS 37.

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?

Response

Subject to our response to question 6 above on contingent liabilities, we agree with the proposal.

Question 8

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?

Response

We agree that goodwill acquired in a business combination should be recognised as an asset.

We believe that adoption of an impairment-only approach as proposed by the Board, is to be welcomed, because it will have the considerable advantage of removing what is very often the quantitatively largest divergence between IFRS and US GAAP net income and equity. It seems unlikely that the FASB would re-align with IAS 22, and the elimination of this significant difference would remove one excuse for the SEC not proceeding faster with acceptance of IFRS financial statements for foreign registrants.

However, we believe that consideration should be given to retaining amortisation of goodwill where the life of goodwill can be shown to be finite rather than indefinite, for example where there is evidence of a time limit on the ability to derive economic benefits from controlling another entity.

Question 9 – Negative goodwill

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?

Response

We believe that one exception should be made to the principle of recording negative goodwill immediately as income, namely where it is identified as reflecting the estimated value of contingent liabilities not reflected in the provisional purchase accounting (see our response to Question 6). It would be released in income during the allocation period as the contingent liabilities met the IAS 37 criteria for recognition. Any balance remaining at the end of the period would be credited to income.

In addition, we would make a plea for retention of the term "negative goodwill", on grounds of simplicity. If the words "negative goodwill" are no longer favoured for whatever reason, we would prefer "discount on acquisition" to the complex wording used in the ED.

Question 10– Completing the initial 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?

(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?

Response

Adjustments to estimates of the total cost of the combination can normally be made within 12 months of the acquisition date. However, in some circumstances (e.g. fair values impacted by regulatory and fiscal requirements which can sometimes take more than 12 months to resolve) extra time is highly desirable for arriving at correct values, and we would suggest that some possibility should be left open to permit taking such items into account, on a very restrictive basis, if resolved by the end of next full accounting period.

Thereafter adjustments should only be made to correct an error (as proposed).

Other Comments

Definition of goodwill

The ED defines goodwill as future economic benefits from assets that are not capable of being individually identified and recognised. It would seem preferable to us to re-word this definition in terms of goodwill being future economic benefits arising from the right to control an entity. Against the definition in the ED, a counter argument could be made, pointing out that because none of the assets which make up goodwill can be recognised under the framework, goodwill itself should not be recognised as an asset for precisely the same reason. The legal right to control an entity, however, does give access to economic benefits over and beyond the right to control the individual assets of that entity, as described in paragraph BC97 of the Basis for Conclusions to the ED. In our view, this right should be recognised as an asset. Also, benefits from this right will potentially continue indefinitely until the acquiring entity decides to dispose of it, so that this alternative definition appears consistent with the impairment-only goodwill accounting model proposed in the ED.

Disclosure requirements

We would ask the Board to clarify whether paragraphs 73 to 76 require disclosure of comparative information.
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C. Answers to the IASB's Specific Questions on ED of 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?

Response

In our view, to prevent unnecessary work, all annual impairment tests should be allowed to be performed at the same date, being any date during an annual reporting period, provided that, where this date is not the balance sheet date, additional testing is performed on any assets for which an indication of impairment arises after the annual test but before the balance sheet date. The requirement in paragraph 8A (a) of the ED that indefinite life intangible assets should be tested at the balance sheet date, should be removed to allow testing of those assets at the same date as goodwill if that date is earlier than the balance sheet date.

Question 2 – Intangible assets with indefinite 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?

Response

We agree with the proposal.

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?

(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?

(c) is the additional guidance in proposed Appendix B to [draft] IAS 36 on using present value techniques in measuring an asset's value in use appropriate? If not, why not? Is it sufficient? If not, what should be added?

Response

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 or consistent with ED3's requirements. A main feature of impairment testing is to base cash flow projections on most recent forecasts established by management, and these should reflect relevant information only. The reasons why management's past estimates of cash flows may have differed from actual cash flows may well be irrelevant to the current forecasts. Also, it is unclear how in practice past differences between management's forecasts and actual cash flows could be taken into account. For these reasons, this requirement should be removed.

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?

(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?

(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?

Response

a) We agree with the requirement in paragraph 74 of the ED that the level at which goodwill is tested for impairment should never be higher than the entity's primary reporting segments.
However, given the way in which FAS 142 is being applied, it is by no means clear that the requirement in the ED to allocate goodwill to the lowest level at which management monitors the return on the investment in that goodwill, would allow an entity reporting under both IFRS and US GAAP to perform the impairment tests at the same level. This may depend on the level of "management" which is monitoring the return, and this level appears not to have been defined in the ED. For Syngenta, the ability to converge exactly with FAS 142 on this point is essential in order to avoid an extremely burdensome duplication of impairment testing. Other entities which report under IFRS, but not under US GAAP, may not have this consideration. Instead of adopting a prescriptive approach, the entity should have discretion to determine the most appropriate organisational level to which to allocate goodwill (but not higher than primary reporting segment), as long as it uses the same allocation basis and level consistently - both within a primary reporting segment and from one reporting period to the next.

b) We suggest that an exception to the proposed approach should be permitted where goodwill in a CGU can be clearly and unambiguously be identified with a retained part of the CGU.

(c) Please refer to (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?

(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?

(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?

Response

(a) We agree.

(b) and (c) - the proposed two-step impairment testing process model is closely modelled on the similar requirements in FAS 142. We wholeheartedly welcome the Board's intention to converge as closely as possible with US GAAP in this respect. However, total convergence is extremely difficult to achieve. The FAS 142 process, unlike IAS 36, is restricted in scope to goodwill and indefinite life intangibles – other long lived assets are tested under a different standard, FAS 144, according to a process which is not convergent with IAS 36 (because FAS 144 requires an initial test based on undiscounted cash flows). In our view, IFRS US GAAP differences will still result from the requirement in paragraphs 85 (c) and 103 of the ED, to recognize any remaining excess of the CGU carrying amount over its recoverable amount, as an impairment loss prorata against other assets in the CGU. Under the requirements of paragraph 104 it may or may not be possible to allocate this excess, in part or totally, for IFRS purposes, because some or all of the other assets in the CGU may have net selling prices greater than their carrying amounts; at the same time, the FAS 144 undiscounted cash flow test may mean that no impairment can be recorded against the other assets in the CGU for US GAAP purposes.

We are also aware that those entities for whom US GAAP reporting is not relevant have serious concerns about the complexity and cost (where independent valuations of assets are required) of the proposed two step process in cases where the first, screening step indicates the need for further work. One alternative approach to the proposed two-step process would be to retain the existing one-step process, under which the excess of CGUs' carrying amounts over their recoverable amounts would be recorded directly as an impairment against the carrying amount of goodwill and then other assets, without moving to the fair valuation allocation process of step 2. This approach would of course be less convergent with US GAAP than the proposals in the ED. A second possibility is to simplify the fair valuation process, in order to reduce the work involved in the second step of the impairment test – for example, to allow the fair values of those assets which do not have a clear and easily available market price to be determined by allocating the recoverable amount of the CGU (adjusted to remove those assets and liabilities with known fair values) to those assets in proportion to their carrying amounts. In our view, either of these alternatives would address the concerns of those entities for whom US GAAP reporting is not relevant.

Question 6 – Reversal 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?

Response

Goodwill impairment losses should be reversed if the reversal represents the correction of an error as opposed to a change in estimate.

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?

Response

We agree with the disclosure requirements in paragraph 134 (a) to (c). We also agree that this information could be given for individual material assets or CGUs under the principle in paragraph 137.

The disclosures in paragraph 134 (d) to (f), and in paragraph 137 as far as they correspond to it, should be removed from the disclosure requirements because:

- they are commercially sensitive and disclosure would damage the reporting entity and therefore its shareholders also.
- The disclosures in paragraph 137 may well prejudice the entity's position in any litigation or potential litigation related to the areas of its business about which the disclosures are made.
- They would be unwieldy in cases where recoverable amounts for different CGUs within a segment or segments have been determined differently (some by net selling price and others by value in use), leading to long disclosures.
- We assume that the requirement to discuss management's past experience in forecasting cash flows is intended to assist users of the financial statements to make a judgement about whether eventual outcomes are likely to differ from current forecasts. In our view, this requirement is inappropriate. A requirement within an *auditing* standard that an entity's auditors should have regard to management's past experience in forecasting cash flows when auditing impairment calculations would be perfectly reasonable. A requirement within an accounting standard to comment on the accuracy of past forecasts used to prepare previous years' financial statements, however, is not relevant to the current financial statements unless comparative figures have had to be restated to correct errors in the original forecasts. Actual cash flows will always be different from forecasts for many reasons which are outside the control of management. Also, in a changing business environment, past performance may not be a good guide to future prospects. Significant variances between forecasts and actual cash flows, or the absence of such variances, may therefore be a poor indicator of whether the original forecasts were biased or unbiased. They may also be a poor indicator of the likelihood, direction or extent of possible future variances between current forecasts and eventual outcomes, and could be misleading. In our experience, in many cases it is not possible to reconcile or even explain the differences between actual and forecasted cash flows, even if the original forecasts were well documented, because in complex businesses and markets, the number of variables which change over time is too great. Changes in the entity's product range, its reporting and organizational structure, and even in the individuals responsible for preparing forecasts, can make it impossible to provide a full audit trail.
- The disclosures far exceed what is required in FAS 142 or FAS 144.

We suggest that the disclosure requirements are modelled on those in FAS 142 and FAS 144. If full benefit is to be derived from convergence, it should extend not just to required accounting treatment, but to disclosures as well.

Other comments

Future "improvement/enhancement" capital expenditure

Paragraph 37(b) of the ED proposes to exclude capital expenditure from the future cash flow forecasts if it will improve or enhance the asset in excess of its standard of performance assessed immediately before the expenditure is made. We do not understand how this requirement, as worded in the ED, could be implemented in practice. If this expenditure is expected to be made at some future date, the asset's standard of performance at that date is unknown, because it could be changed by future events. We are unsure whether the standard of performance which the Board intends to refer to is that which the asset *is expected to have at the time the expenditure is expected to be made,* based on currently available information. In our view, it would be more appropriate and logical to refer to the standard of performance at the date of the impairment calculations.

D. Answers to the IASB's Specific Questions on ED of amendments to IAS 38

Question 1

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?

Response

We agree that these criteria are appropriate.

Question 2

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.

Response

In our view, it is only possible to recognise items as acquired intangible assets if it is possible to measure their fair value using a method that is generally accepted as reliable and appropriate in the circumstances. It is not possible simply to assume as a given that an item can be measured reliably. Fair value can be determined either by reference to external markets, present value techniques based on future cash flows, established techniques used by a qualified specialist valuer, or by direct evidence from documents related to the business combination. We believe that if a fair value cannot be determined satisfactorily in any of these accepted ways, any fair value allocation would be arbitrary.

With regard to in-process research and development (IPR&D), we agree that it is possible to determine a fair value reliably. However, the proposed accounting treatment – capitalization of acquired IPR&D – is not convergent with the existing US GAAP requirement, which requires immediate expensing if acquired IPR&D has no alternative use. We understand that the FASB intend to change the existing requirement to converge it with the approach suggested in the ED. As our major concern is convergence, our support for the proposals in the ED on IPR&D is conditional on the FASB also adopting the proposed treatment, and on the ability to delay adopting that treatment for IFRS until the FASB has issued an official pronouncement containing this change.

Question 3

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?

Response

We agree with the proposal.

Question 4

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)?

Response

We agree with the proposal.

Question 5

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?

Response

We agree with the proposal.

Other comments

Directly attributable expenditures

We are aware that the proposal to delete paragraph 58 (d) – paragraph 54 (d) of the existing IAS 38 – is in line with the changes proposed in the improvements project. However, in our view, there is no reason to remove this paragraph, and it should be retained.