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Our Ref BRS/RWC

International Accounting Standards Board
30 Cannon Street
London
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United Kingdom

For the attention of Annette Kimmitt

4 April 2003

Dear Sirs

ED 3 BUSINESS COMBINATIONS AND PROPOSED REVISIONS TO IAS 36 AND IAS 38

Grant Thornton welcomes the opportunity to comment on the proposals set out in the above Exposure Drafts. In this letter, we set out the comments of our international organisation.

We believe it is essential that the Board produces practical, workable standards that can be applied around the world by a wide range of reporting entities. We are not convinced that the proposals set out in these Exposure Drafts meet this basic requirement. In our detailed comments, we identify specific areas that we believe will be difficult or costly to implement, together with our suggested improvements.

We strongly oppose the proscription of goodwill amortisation in all cases, and believe that it should continue to be required where goodwill has a finite useful life. In many cases, we believe that this will provide more relevant and reliable information to users of accounts.

We question the practicability of separating out intangibles on acquisition to the extent envisaged in the Exposure Draft and we believe that this will not necessarily provide reliable information to users.

We believe that the Board should not close out Phase I of its business combinations project until it has consulted on Phase II as, in our view, the standards from both phases should be developed together, not in isolation from each other.

We respond in detail to the questions raised in the Exposure Drafts in the appendix. If you would like us to amplify our comments, please contact Robert Carroll on +44 (0)870 991 2210.

Yours faithfully

Grant Thornton

APPENDIX 1

ED 3 BUSINESS COMBINATIONS

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?

We agree with the proposed scope exclusions. However, we are concerned that some proposals in Phase I of the Board's project may be affected by Phase II proposals. ED 3 paragraph 78 delays implementation for mutual entities and the bringing together of entities only by contract (for example, to form a dual-listed corporation). Unless these and the exemptions in paragraphs 2 and 3 are the only possibilities being considered for another method, such as fresh start accounting, we foresee a risk of multiple changes in requirements for a particular type of transaction, leading to ongoing inconsistency in reporting (as retrospective application will not be mandated). For example, combinations involving mutual entities are often currently accounted for under the pooling of interests method, which will be superseded upon issuance of the final IFRS. However, due to the delayed implementation, those entities will not be subject to the requirements of the IFRS. How should those entities account for combinations occurring between the effective date of the IFRS and the issuance of guidance on the application of the purchase method to those transactions? We therefore believe that the IASB should try to introduce new standards in respect of phases I and II of its business combinations project from the same effective date, if possible, to avoid any transitional issues between the two phases, or should ensure that the guidance on pooling of interests accounting remains available to those combinations that are excluded from the scope of this proposed IFRS until Phase II is completed.

It is not clear to us how the part of the scope exclusion referring to "business combinations in which separate entities or operations of entities are brought together to form a joint venture" might differ from a pooling of interests. Is this exemption intended to cover a situation where a top company is put over two separate companies, where the shareholdings resulting were supported by a shareholder agreement? If so, would it still be possible to use the pooling of interests method in such cases? This issue does not appear to fall within the scope of a project on common control and it would be helpful if the Board were to clarify the intention of this exemption.

(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 are concerned that the definition of common control may be too narrow.

ED 3 paragraph 10 appears to restrict the common control scope exclusion to situations where there is a contractual arrangement between the parties. Therefore, business combinations where two entities have the same shareholders and proportional interests, but no contractual arrangement, do not appear to be excluded from the scope of the proposed standard. If the entities are combined into a group, there will in substance be no acquisition. However, the proposed standard seems to force the identification of an acquirer and the recognition of goodwill, unless the shareholders create a contractual relationship first, which may involve undue cost or effort and which would serve only as a device to bring a combination within the scope exemption.

ED 3 paragraph 22 addresses a combination effected by means of a newly incorporated entity and states that one of the existing entities should be identified as the acquirer. However, it does not address how to deal with the combination of that acquirer with the new entity. As no elaboration is provided, it is not clear what kind of transaction this paragraph is addressing. For example, is this paragraph intended to cover situations where a combination is effected by means of a new parent entity set up to issue shares in a share-for-share exchange to acquire two existing companies? Is it implying that the combination between the existing entity identified as the acquirer and the newly incorporated entity should be treated as a common control transaction? It would be helpful if the Board could clarify its intentions by providing some illustration, and indicate how the combination of the acquirer and the new entity should be accounted for.

The proposed standard does not address how to account for the addition of a new parent company on top of an existing company or group, where the shareholders simply exchange their existing shares for shares in the new parent. This is a common type of transaction in some jurisdictions, for example, where a new public company is added on top of an existing private company to effect a flotation. As with the combination of two entities with the same shareholders and shareholdings, in substance there will have been no business combination. At present, such transactions are often accounted for by using the pooling of interests (or merger) method. If the intention were to exclude such a transaction from the definition of a business combination, it would be helpful if this were made clear. If such a transaction is not to be excluded from the scope of the proposed standard, we suggest that the standard should indicate that it should be dealt with as a reverse acquisition.

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?

We agree with the proposed elimination of the pooling of interests method of accounting for business combinations, as we believe that true mergers are extremely rare and do not merit a different treatment from other business combinations.

We understand that combinations currently accounted for as poolings (such as those involving mutual entities) may subsequently fall within the scope of fresh start accounting. Given the exclusion of those entities from the scope of this proposed IFRS, we believe it is undesirable for the guidance on poolings to be abolished for such combinations before the issue of whether they will be covered by fresh start accounting has been resolved. We therefore believe that the Board should either complete its deliberations on the potential use of fresh start accounting before abolishing the pooling method or determine the scope of any potential application of fresh start accounting and ensure that the scope exclusion from this proposed standard aligns with that scope.

We are also concerned that, in a small number of cases, identifying a controlling party in combinations currently accounted for as poolings may be very difficult and potentially arbitrary. We suggest that the Board conducts some form of field-testing of its proposals. For example, they could be applied to recent combinations that have been accounted for as poolings under an existing national standard that uses the 'no dominant party principle' to identify poolings, such as the current UK standard. The purpose of such a field test would be to ascertain whether an acquirer could be identified satisfactorily in all cases, or whether additional guidance on identifying an acquirer would be helpful.

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 support the Board's proposals in principle. However, it appears to us that the Board's proposal on this point omits to deal with the issue of the shareholdings in the combining entities. If the shareholders of one entity are entirely different to those of the other, the description of the circumstances in which a combination should be accounted for as a reverse acquisition appears to be appropriate. However, where the combining entities have shareholders in common, the picture may change according to whether the identity of the shareholders is taken into account.

For example, suppose that Entity A has 100 shares in issue and Entity B has 200 shares. A single shareholder holds 60% of A and 46% of B. If A then issues shares to the shareholders of B in a one-for-one exchange, the former shareholders of B will hold 200 shares out of 300 in the enlarged A. Hence, without considering the identity of the shareholders, it appears that B has acquired A in a reverse acquisition as B's former shareholders now hold the majority of A's shares. However, if one considers the identity of the shareholders, it becomes apparent that the former controlling shareholder of A, who also held a minority stake in B, now holds 50.67% of the enlarged A, and thus retains control. Hence, the effect is really that A has acquired B.

ED 3, paragraph 21 states that "all pertinent facts and circumstances shall be considered…" which could be taken to include considering shareholders in common, though this is not made clear. We are aware of an example in the UK (HBOS plc) where the disposition of institutional shareholdings was used to rebut a presumption of dominance in FRS 6, thus enabling a combination to be accounted for as a merger. We are concerned that similar issues may arise in marginal cases when attempting to identify whether a combination is an acquisition or a reverse acquisition, and we suggest that the Board should consider the need for additional guidance on this point.

If the Board's intention is that the identity of shareholders should be a pertinent fact, the proposed wording could be amended to make it clear that a reverse acquisition occurs where the former shareholders of the legal subsidiary have the power to govern the financial and operating policies of the other entity.

(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?

We find the proposed guidance appropriate and helpful. Other than our comments under (a) above, we have no suggestions for further specific guidance.

Question 4 – Identifying 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?

The need always to identify one of the existing entities as the acquirer follows from the abolition of pooling. We are concerned that this may be a very marginal decision in some cases, such as where three entities combine via a new parent where the split of shareholdings between the former shareholders of the three entities is, for example, 30:30:40. As with the material on reverse acquisitions, we foresee a need for additional guidance where there are shareholders in common in such situations. In some combinations, it may be very difficult to identify any party as the acquirer, other than arbitrarily. In such cases, fresh start accounting may be appropriate and we suggest that this possibility be explored before the standard based on ED 3 is finalised.

A further potential problem in identifying an acquirer arises where a series of combinations occurs. For example, suppose entity A has 40 shares, entity B has 35 shares and entity C has 25 shares in issue. First, B and C combine by means of a one-for-one share exchange. As B's former shareholders will hold a majority of the combined B and C group ('BC'), B will be acquirer. BC will then have 60 shares so, if A and BC combine via a one-for-one exchange, BC will be the acquirer. However, if the same ultimate combination of A, B and C is achieved by A first acquiring either B or C in a share-for-share exchange, then the enlarged group acquiring the remaining entity, A will be the acquirer of both B and C. The ultimate composition of the group and the disposition of shareholdings will be the same but the accounting will differ.

Our comments in response to Question 2 above regarding identifying a controlling party are also relevant to this question.

Question 5 – 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?

We support this proposal.

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?

We support the proposal for initial recognition of acquired contingent liabilities at fair value. However, we are concerned that the proposed standard omits to deal with contingent assets, which we note from the Basis for Conclusions are to be considered in Phase II. We believe that the arguments in the Basis for Conclusions to the effect that recognition at fair value overrides the 'probable inflow of benefits' aspect of the assets definition indicates that contingent assets should be recognised in a manner similar to contingent liabilities.

We are also concerned that the recognition and ongoing measurement of contingent liabilities at fair value is inconsistent with the Framework, as identified by the Board in paragraph BC82 of the Basis for Conclusions. We therefore encourage the Board to progress its concepts project as soon as possible so that this issue may be resolved.

We note that the Board proposes that the fair value of acquired contingent liabilities should be remeasured subsequent to acquisition. We do not support this proposal as it is inconsistent with both the treatment of other contingent liabilities and the subsequent treatment of other acquired assets and liabilities. We share the Board's objection to subsequent measurement in accordance with IAS 37 (expressed in paragraph BC84 of the Basis for Conclusions). However, we propose that the fair value of acquired contingent liabilities should be treated as 'deemed cost' for subsequent measurement purposes. If, subsequent to initial recognition, the contingency becomes probable such that the IAS 37 requirement for recognising a provision is met, the liability should then be remeasured in accordance with that standard. If the entity is subsequently released from its contingent obligation, we propose that the contingent liability should be derecognised.

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 support this proposal. We observe that, given recent decisions by FASB in the USA, and existing requirements of other standard-setters, the Board's proposal represents a significant step towards global convergence on this issue.

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

We disagree with the proposal that goodwill should be accounted for after initial recognition at cost less any accumulated impairment losses in all cases. We are not convinced that amortisation should be banned outright and we believe that the amortisation approach should be retained, as discussed in more detail below.

For many smaller and middle market entities, the benefits of providing the information derived from annual impairment reviews will be far exceeded by the cost of performing them. In our view, the Board, in order to comply with paragraph 44 of the Framework, should state their reasoning on this issue in the Basis for Conclusions, particularly if the final standard continues to require impairment reviews in all cases. Under our proposals, set out below, many small and medium-sized entities would determine a best estimate for the life of goodwill, and amortise it.

In addition, we believe that where the variability in potential outcomes underlying the value in use calculation is significant (which will be the case in many smaller operations) the information generated by the impairment regime will be less reliable than that generated by the amortisation regime. Consequently, the information provided may not meet the objective and qualitative characteristics of financial statements, as set out in the Framework.

We do not believe that there should simply be a free choice between amortisation and impairment. Instead, we propose the following approach:

- The useful life of goodwill should be presumed to be finite unless there is clear evidence to rebut this presumption and demonstrate durability of the goodwill. The factors to consider in determining the useful life of goodwill, or in determining that its useful life is indefinite, are, in our view, broadly similar to those set out in the Exposure Draft of Proposed Amendments to IAS 38, Intangible Assets, paragraph 87;
- Where goodwill cannot be demonstrated to have an indefinite useful life, it should be amortised over the management's best estimate of its useful life;
- Impairment testing for goodwill with a finite life should be required as follows:
  - Where the useful life is greater than twenty years from initial recognition, annual impairment tests should be conducted. Such a test would act as a protection against an unduly optimistic view of useful life;
  - Where the useful life does not exceed twenty years from initial recognition, a modified first-year impairment test should be conducted at the end of the first full year following the acquisition (as outlined below), and full impairment tests should be conducted subsequently if indications of impairment are present;
- Where goodwill is determined to have an indefinite life, it should not be amortised, but should be subject to annual impairment review.

We propose that the modified first-year impairment test referred to above should comprise two steps. The first step would compare the post-acquisition performance of the acquired business with pre-acquisition forecasts used to support the purchase price. If this first step were to indicate that post-acquisition performance had failed to meet expectations, or if other previously unforeseen events or changes in circumstances have arisen which indicate that the carrying value of goodwill might not be recoverable, a full impairment test should then be carried out. We believe that such a test would identify any potential overpayment or failure to achieve synergies or cost savings identified at acquisition, which were taken into account in the purchase price, and thus gave rise to goodwill.

We comment in more detail on impairment testing of goodwill in our response to questions on the Exposure Draft of changes to IAS 36.

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 contingent 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 have misgivings about an approach that will lead to immediate profit recognition where such an excess occurs. We therefore suggest that the Board reconsiders some form of deferral approach, for example by releasing the excess up to the fair value of the acquired non-monetary assets to the income statement as those assets are consumed or sold. Any remaining excess would be released to income over the periods expected to benefit, on which clear guidance should be provided in the IFRS. However, we acknowledge that the Board's proposed approach will achieve convergence with US GAAP on this issue, which we recognise is an argument in its favour.

If the Board's proposals were to be implemented, we would also be concerned that entities might seek to recognise intangible assets of dubious value and thus create or increase the 'excess', giving rise to an immediate boost to profits. We therefore recommend that the Board should emphasise the need for reliable measurement of unique intangible assets (ie those that lack a reliable market value) and reconsider the possibility of placing some restriction on the amount that may be recognised for unique intangible assets where so doing would create or increase the 'excess'.

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?

We agree with this proposal in principle but suggest that it be more formally linked to an entity's reporting cycle, for example by stating that the revised amounts must be recognised by the first results (interim or full year) reported after the 12-month point.

(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 support this proposal.

Other comments

Interaction with Phase II

We note from recent IASB meetings that the Board's deliberations on Phase II are likely to impact on proposals set out in ED 3, for example those relating to minority interests and step acquisitions. In our view, the Board should not complete its deliberations on Phase I and issue a final standard until it has considered the comments arising from the Phase II exposure draft.

Definition of a business combination

We are aware that issues have arisen in some jurisdictions regarding the distinction between acquiring assets and acquiring a business. The definition of a business combination in ED 3 refers to "the bringing together of separate entities or operations of entities", but this definition is not elaborated on elsewhere in the Draft, in particular the meaning of "operation". In some cases, an individual asset or group of closely related assets may generate cash flows largely independent of other assets and may constitute a business in their own right, whereas in other cases apparently similar assets may not (for example vessels). We suggest that the Board takes into account the issues dealt with in the US EITF Abstract 98-3, 'Determining Whether a Nonmonetary Transaction Involves Receipt of Productive Assets or of a Business' in considering whether to provide additional guidance on the definition of a business combination.

Transitory control and the substance of a combination

We are aware of situations where a business combination has been structured by means of contractual arrangements to ensure that a particular party is treated as the acquirer. In some cases, these contractual arrangements have had a finite duration and their primary purpose has been to achieve an accounting result. We are aware that such arrangements have attracted the attention of securities regulators, who have sought to impose minimum durations on such contractual arrangements. As we favour a principles-based approach, rather than one that is rules-driven, we suggest that the Board considers incorporating additional guidance either into its business combinations standard, or into a future IFRS. This guidance should emphasise that the substance of a combination needs to be considered in determining which party has control, and that arrangements structured to achieve a particular accounting result should be afforded little weight.

Recognition of deferred tax assets after the initial accounting is complete

ED 3 paragraph 64 proposes adjusting the goodwill balance after the initial accounting for a business combination is complete where the potential benefit of the acquiree's income tax loss carry-forwards or other deferred tax assets did not satisfy the criteria for recognition but is realised subsequently. We note from the Basis for Conclusions that the Board has carried forward this provision from IAS 22 and that it intends to revisit it at Phase II. We see no justification for such an exception and we suggest that it be removed.

Disclosures

The extent to which comparative figures will be required is not clear from the proposed disclosures in ED 3 paragraphs 65-76, which implies that the normal IAS 1 requirement for full comparatives for numerical information will apply. In our view, full comparatives for numerical information would be excessive in this case and we suggest that the Board should reconsider the extent to which comparative information should be required. We also believe that the disclosure proposed by paragraph 66(h) is unnecessary and should be deleted.

Transitional provisions

ED 3 paragraph 77 does not specify whether retrospective application of the standard is permitted. We suggest that the Board permits retrospective application of the standards resulting from Phases I and II in a similar manner to that now proposed for business combinations requirements in its proposed standard on first-time adoption of IFRS. This would mean that application to all combinations subsequent to a specific date would be permitted.

Early adoption

We suggest that ED 3 paragraph 84 be amended to require entities that adopt the standard early to state the date from which they have applied it.

Definition of agreement date

We are concerned that the proposed definition of agreement date may be loose. The reference to "substantive agreement" rather than binding agreement suggests that there might be scope for entities to change their minds after agreement date, then possibly change again, thus moving the agreement date.

Consequential amendment to joint control definition

We disagree with the proposed consequential amendment to IAS 28 and IAS 31 to change the definition of joint control. In our view, unanimous consent in all financial and operating decisions is not necessary for joint control to exist. Joint control is the contractually agreed sharing of control, which means that no one venturer can control the joint venture but all together can do so. We believe that unanimity is necessary only for important strategic issues but not for detailed operational matters, where it may be impracticable in any event, particularly where one of the venturers handles the day-to-day operations of the venture.

We see no reason for this proposed change to be made at this stage and we are concerned that the Board has proposed a substantive change such as this as a consequential amendment, without proper explanation.

PROPOSED AMENDMENTS TO IAS 36 IMPAIRMENT OF ASSETS

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 support the proposals to test intangible assets with an indefinite life and goodwill that is not amortised for impairment at least annually.

We do not understand the rationale for requiring the annual test to be at the end of the reporting period for intangible assets (paragraph 8A) but permitting it to be carried out at any time during the period for a cash-generating unit to which goodwill has been allocated (paragraph 93). Performing tests at different dates is likely to involve duplication of effort as, in many cases, intangible assets will need to be tested as part of a cash-generating unit, leading to overlap between the goodwill and intangible asset impairment tests. We believe that the most relevant information will be provided if the annual tests are carried out at the end of the reporting period for both intangible assets and goodwill. However, we recognise that this may not be practicable, especially where external expert involvement is required. Therefore, we suggest, as an alternative, that the tests could be performed at the same time during the reporting period for both goodwill and intangible assets, with checks similar to those in paragraph 96 of the draft standard being applied to assess whether tests conducted earlier in the current period remain valid at the year end.

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 that intangible assets with indefinite lives should be treated on a basis consistent with other assets.

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?

We agree with the elements identified in paragraph 25A. We also agree that an entity should be permitted to reflect those elements either as adjustments to future cash flows or adjustments to the discount rate.

(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?

We agree in principle with this proposal but question whether it has any practical outworking. It is not clear to us how management's past ability to forecast cash flows accurately is to be taken into account in the assumptions supporting the cash flow projections, although we acknowledge that poor previous forecasting performance might be evidence supporting the unreliability of current estimates.

(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?

We believe that the additional guidance is appropriate and will be helpful. We consider it impracticable for the IASB to cover every conceivable point on using present value techniques in an appendix to a standard and we do not see any need to add further material, except with regard to the discount rate. The selection of an appropriate discount rate is a subjective and difficult process, and potentially introduces significant unreliability into the information produced. We therefore suggest that the Board considers providing further guidance, for example on the use of, or adjustments to, an entity's weighted average cost of capital in impairment calculations.

We note that Appendix B is to be an integral part of the standard. Consequently, in accordance with the 'Preface to International Financial Reporting Standards', this material will be mandatory. We are not convinced that material that is described in the introduction to Appendix B as "guidance" should have such status. We therefore suggest that the Board should reconsider whether any material that they believe should be mandatory should be retained within the main body of the standard, with Appendix B providing additional implementation guidance outside the mandatory text.

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?

We support the Board's proposal for the reasons given in the Basis for Conclusions.

(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 that goodwill associated with such an operation should be included in determining the gain or loss on disposal. We also agree that the amount of the goodwill should be measured based on the relative values of the operation disposed of and the portion of the unit retained, but only if no more rational and systematic basis of allocation can be identified. For example, we question whether the proposed approach will produce sensible results where a loss-making part of an otherwise profitable cash-generating unit containing goodwill is sold. In such a case, we doubt that it would be sensible to allocate any goodwill to the portion sold.

(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 support the Board's proposal for the reasons given in the Basis for Conclusions.

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 this proposal, though we note that it differs from the current US GAAP approach, which uses fair values for step one of the goodwill impairment test.

(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?

Our comments in response to this question are combined with those for point (c) below.

(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 understand the arguments that the Board has set out for adopting the proposals referred to in questions 5(b) and 5(c). However, we are concerned that the two-step test as set out in the proposed standard will produce illogical and unsatisfactory results in some cases, particularly where the recoverable amount of a cash-generating unit is close to its carrying value.

The following examples illustrate our concerns regarding potentially illogical results:

	Case A	*Case B*
Carrying value of other assets	110	110
Carrying value of goodwill	40	40
Carrying value of cash-generating unit	150	150
Fair value of other assets	120	120
Implied value of goodwill	25	35
Recoverable amount of unit	145	155

In Case A, the recoverable amount of the unit is marginally below carrying value, thus indicating a potential impairment under the screening mechanism. The second stage test measures the impairment loss for goodwill as the difference between its implied value and its carrying value, giving rise to a loss of 15. This is greater than the impairment loss identified by comparing the carrying value of the unit with its recoverable amount, where the loss is only 5. The difference arises because the unrecognised increase in value of the other assets of 10 is not allowed to cushion the fall in value of goodwill, for the reasons set out in paragraphs C33-C36 of the Basis for Conclusions. We are not convinced by the Board's arguments on this point as we consider it illogical to write down a cash-generating unit to below its recoverable amount by excluding a cushioning effect in this situation when other 'cushions' are built into the impairment test (as discussed in the Basis for Conclusions).

By contrast, in Case B the screening test does not identify an impairment, even though stage two of the test, if it were performed, would identify that the implied value of goodwill is below its carrying value. Thus, in this case, the increase in the fair value of other assets is permitted to cushion the loss in respect of goodwill.

We do not see why an impairment loss should be recognised in Case A when no impairment loss is recognised in Case B, despite the fact that the implied value of goodwill is below carrying value in both cases. We believe that the result in Case B contradicts the Board's reasoning, as set out in paragraphs C33-C34 of the Basis for Conclusions, for not allowing unrecognised value in identifiable assets to provide a cushion against the recognition of an impairment loss for goodwill. We note that the Board has addressed this issue in paragraph C49, where it states that if the value of identifiable assets is being maintained, it is likely that the value of goodwill will also be maintained. We are not convinced that this is necessarily true as, for example, the fair value of identifiable assets may increase because of a rise in property prices whilst the goodwill in the business is still impaired. We concur with the alternative view expressed in paragraph AV17 of the Basis for Conclusions to ED 3 that the Board's assertion in paragraph C49 is unsupported by evidence.

We believe that the apparent anomalies identified by the above examples may result from the difference in approach of the first stage of the impairment test, compared to the US GAAP approach, whilst using a similar test for stage two. As we support the IAS 36 approach to impairment testing in general, we believe that the Board should reconsider whether the consistency between the impairment test for goodwill and the test for assets can be improved, for example by adopting a one-step approach applying the current IAS 36. However, if the Board considers it necessary to retain its proposed two-step approach, we propose that the total impairment write-down should be limited to the recoverable amount of the cash-generating unit in a situation such as Case A in the above example.

We believe that the requirement to measure the identifiable assets and liabilities of a cash-generating unit at fair value when stage two of the impairment test is performed will make the impairment test unduly complex and burdensome for many businesses. We concur with the alternative view expressed in paragraph AV18 of the Basis for Conclusions to ED 3 that the existence of various 'cushions' against impairment makes it doubtful whether the two-stage test actually achieves sufficient rigour to justify its complexity and cost.

We also believe that the costs of performing the impairment tests may outweigh the benefits of doing so, even allowing for cost savings resulting from the screening test and the use of previous calculations. For unquoted entities in particular, there seems to be little merit in mandating the form of annual impairment test proposed, or even a simpler one-stage test, when there is likely to be little, if any, incremental benefit to users of the accounts compared to amortising goodwill. This constitutes another reason why we recommend, in our comments in response to ED 3 above, that the Board should not proscribe the amortisation of goodwill in all cases.

We support the alternative view in paragraph AV23 of the Basis for Conclusions to ED 3 that the Board is putting its faith in a potentially unreliable and certainly complex test, and that until greater experience has been accumulated, it cannot be established that such tests pass the cost/benefit test for the majority of entities affected.

We are concerned that the Board's desire to adopt its proposed approach to impairment testing of goodwill, and prohibit goodwill amortisation, may be driven more by a desire to achieve international convergence than to achieve its objectives, as set out in the Preface to International Financial Reporting Standards. We therefore suggest that the Board carries out research to ascertain how well the two-step approach currently in SFAS 142 is working in practice, in terms of practicality, cost, reliability and credibility for users and preparers, before incorporating a similar approach into IFRS.

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 support the Board's proposals to prohibit the reversal of goodwill impairment losses, for the reasons set out in the Basis for Conclusions.

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?

We consider that the proposed disclosure requirements are excessive. We believe that the costs of disclosing all of the information listed in paragraph 134 are likely to exceed the benefits obtained. Where a business has made a large number of acquisitions, the disclosures are likely to be very long, leading to information overload, as a result of which the information may lose its value. We also note that some of the information listed is likely to be commercially sensitive and we are not convinced that there are sufficient grounds to mandate its disclosure.

Specifically, we suggest deleting the following proposed disclosures:

- the amount by which recoverable amount exceeds carrying amount under sub-paragraph (d);
- information relating to the key assumptions under sub-paragraphs (e)(i) and (iv) and (f)(i) and (ii); and
- information relating to changes in projected growth rates under sub-paragraph (e)(v).

We also propose that the Board should consider making more allowance for aggregation of information in the proposed disclosures, so that the main points of interest to readers of the accounts are not obscured by excessive detail.

(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?

Subject to our comments under (a) above, we concur with this proposal.

Other points

Wording of paragraph 103

We find the wording of paragraph 103 of the proposed revised IAS 36 unhelpful. In our view, the phrase "impairment loss shall be allocated" is vague. It is not clear whether the "impairment loss" means the difference between the carrying amount of a cash-generating unit and its recoverable amount (as implied by paragraph 103) or the difference between the carrying value of goodwill and its implied value (as implied by paragraph 85). As illustrated in the example above, this latter number may be greater than the former. We suggest that this paragraph be reworded to clarify the meaning of the term "impairment loss".

Subsequent monitoring

We note from paragraphs C72-C75 of the Basis for Conclusions that the Board has rejected the suggestion of including a subsequent cash flow test (along the lines of that in FRS 11 in the UK) in the proposed revised IAS 36. The Board notes arguments in favour of such a test in paragraph C73 and sets out arguments against such a test in paragraph C74. However, in our view, the arguments in paragraph C74 do not rebut those in paragraph C73.

We concur with the alternative views expressed in paragraphs AV13-AV16 in the Basis for Conclusions in ED 3. We believe that some form of subsequent monitoring test provides an important reality check on the estimates used in impairment calculations, even if it lacks theoretical purity. In addition, we do not accept the Board's argument that the subsequent cash flow test is designed only to prevent entities from avoiding goodwill write-downs. This is not how the test in the UK FRS 11 is set out and it is not restricted to goodwill impairments. We also doubt the validity of the Board's argument that the bigger risk is of entities trying to write off goodwill without adequate justification. We believe that the risks of using over-optimistic estimates to avoid an impairment write-down are at least as significant, if not more so.

We believe that disclosures, no matter how extensive, cannot provide the same quality of test of the estimates used in impairment calculations as a subsequent cash flow test, even if such a test is theoretically impure.

Reorganisations

We acknowledge that the Board is not reviewing IAS 36 in detail at present. We nevertheless recommend that the Board considers whether paragraphs 37-39 should be revised to allow anticipated reorganisation costs and capital expenditure to be taken into account in the impairment calculations in the case of a newly acquired cash-generating unit. It is common for such anticipated costs to be taken into account in determining the purchase price of the unit and for such costs to be necessarily incurred in order to obtain the benefits from the investment. It therefore appears logical to take the costs into account in the impairment calculation.

PROPOSED AMENDMENTS TO IAS 38 INTANGIBLE ASSETS

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?

We support this proposal in principle but we have serious concerns about whether some of the intangible assets listed in the Draft Illustrative Examples in ED 3 can realistically be identified and measured with sufficient reliability to merit recognition in the financial statements, for example trade dress and non-contractual customer relationships.

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.

Our response to this question is divided into four sections:

- reliability;
- closely related intangibles;
- cost/benefit issues;
- review of US experience.

Reliability

We support the principle that intangible assets should be identified separately from goodwill on a business combination wherever practicable as we believe this enables the reader of the accounts to gain a better understanding of an acquisition and of management's subsequent stewardship of the assets. However, we do not believe that sufficient information can reasonably be expected to exist to measure reliably the fair value of an intangible asset acquired in a business combination in all cases.

We note that paragraph 38 of the proposed revised IAS 38 states that, "An entity will be unable to measure reliably the fair value of an intangible asset when comparable market transactions are infrequent and alternative estimates of fair value (for example, based on discounted cash flow projections) cannot be determined." We believe that this scenario will arise frequently with intangible items identified in a business combination involving early-stage enterprises, those with little or no product history, or with non-comparable product or service offerings or ideas. In our view, the Board should apply a similar restriction on the recognition of intangible assets separately from goodwill in a business combination.

Closely related intangibles

We observe that the Draft Illustrative Examples to ED 3 include the statement, "An entity is not precluded from recognising a group of complementary intangible assets commonly referred to as a brand as a single asset, provided the assets that make up that group have similar useful lives." We propose that this statement be transferred to the main body of the standard, or otherwise given greater prominence, as we support the principle that it encapsulates, ie not recognising every conceivable intangible asset separately if they cannot realistically be separated from each other and if separate identification would not add value to the information provided in the financial statements.

For customer-related intangibles, the values of customer contacts and relationships, order backlogs and customer lists are all likely to depend on the same underlying cash flow streams. Hence, there is a risk of double counting and thus recognising, in effect, the same asset two or three times. We therefore believe that it may be more sensible to aggregate such items, if they have similar useful lives, as a single intangible asset representing customer relationships, provided that such an asset can be measured reliably. We are also concerned that similar double-counting problems may arise with technology-based intangible assets.

In our view, it is also often extremely difficult to identify cash flows from some intangibles, such as trade dress, and thus to measure fair value reliably and separately from other closely related intangibles such as brand names or secret formulas. Generally, an intangible such as trade dress is not separable and cannot be valued independently of the product or service to which it relates. Therefore, we propose that such items may be subsumed within a larger intangible asset representing a brand, or, if such an asset cannot be measured reliably, subsumed within goodwill, except in the rare cases where they can be clearly distinguished and reliable valuation can be obtained.

We question whether all items listed in the Draft Illustrative Examples to ED 3 can even be said to be assets, in particular such uncertain and potentially ephemeral items as non-contractual customer relationships. We doubt whether such relationships meet the definition of an asset, as we do not see that the entity has any control. Even if the entity were seen to have control over, and could sell, information about the non-contractual relationship, it is doubtful that the value of the information would be the same as the perceived value of the relationship, and neither may be capable of reliable determination. Therefore, we question the value of the information provided by recognising such items separately from goodwill.

We note that the list of intangible assets set out in the Draft Illustrative Examples to ED 3 is similar to that already included in US GAAP. We are concerned that some regulators have taken the equivalent US GAAP list very literally as a list of intangibles that should be recognised separately if they exist. In our view, such an approach is undesirable and we urge the Board to emphasise that any list that it provides is nothing more than an illustration of the kind of intangible assets that might be identified, if they can be measured with sufficient reliability.

Cost/benefit issues

Even where sufficient information does exist to measure reliably the fair value of intangible assets acquired in a business combination, the costs of measuring fair value with sufficient reliability may exceed the benefits obtained from so doing. We are particularly concerned about the difficulties that unquoted and smaller quoted entities are likely to face in determining the fair value of acquired intangibles, given that they are unlikely to have highly sophisticated accounting resources. We therefore propose that, where the costs of determining with sufficient reliability the fair value of acquired intangibles exceeds the likely benefit to be obtained, the standard should permit such items to be subsumed within goodwill.

We also suggest that the Board should address materiality in its proposed standard, by stating that intangible assets need not be identified separately from goodwill if the resulting information is not material.

In addition, if amortisation of goodwill were to be permitted, the scope for arbitrage between goodwill and intangible assets would diminish, as would the pressure to identify every conceivable intangible, regardless of the cost of so doing.

Review of US experience

As we have commented in our response to the proposed changes to IAS 36 (question 5) we are concerned that the Board is proposing to adopt the requirements of recently issued US GAAP standards apparently without assessing how well those standards are working in practice. We are aware that significant measurement difficulties are arising under SFAS 141, even for the largest and most sophisticated entities. FASB has had to issue numerous pronouncements as a result of implementation questions put to it, and the AICPA has issued valuation guidance. We therefore suggest that the Board conducts research into practical application issues arising from the recent US standards before adopting a similar approach.

More generally, we believe it is essential that the IASB produces practical, operational standards. There is a danger that writing complicated standards that are difficult to follow will lead to criticism of preparers who are considered not to have followed them properly. This could lead to a reduction in the credibility of, and confidence in, International Financial Reporting Standards as a whole – a result that would benefit no one in the quest for transparent, high-quality global financial reporting.

As an additional observation, in our view the Board's assertion that the probability recognition criterion will always be satisfied effectively amounts to the abolition of this criterion in an acquisition situation.

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?

We agree that the useful life of an intangible asset may be regarded as indefinite, based on the circumstances set out in the Exposure Draft. However, we foresee potential difficulties in distinguishing between assets where the useful life is finite, but hard to determine, and those where it is indefinite, and suggest that the Board reconsiders the need for further guidance on this distinction.

We do not support the removal of the requirement for annual impairment tests for intangible assets with long, but finite, useful lives. We are concerned that entities may estimate useful life to be very long, but not indefinite, and thus avoid having to carry out annual impairment tests. Useful lives of intangible assets are often subjective and difficult to estimate. We therefore believe that the current requirement for annual impairment tests where useful life exceeds twenty years from initial recognition provides a valuable safeguard against over-optimistic estimation of useful lives. Consequently, we favour retaining a requirement for annual impairment testing of intangible assets with finite useful lives exceeding twenty years from initial recognition.

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)?

We support this proposal for the reasons given in the Basis for Conclusions.

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?

We support this proposal.