



**International
Accounting
Standards
Board**

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These notes are based on the staff papers prepared for the IASB. Paragraph numbers correspond to paragraph numbers used in the IASB papers. However, because these notes are less detailed, some paragraph numbers are not used.

INFORMATION FOR OBSERVERS

Board Meeting: 22 July 2008, London

Project: Amendments to IFRS 5

Subject: Sweep Issues (Agenda Paper 4)

PURPOSE OF THIS MEETING

1. The purpose of this meeting is to resolve all remaining issues that need to be addressed before issuing an Exposure Draft to amend IFRS 5, *Non-current Assets Held for Sale and Discontinued Operations*.
2. This memorandum is structured as follows:
Issue 1: Additional Criteria for the Definition of Discontinued Operations
Issue 2: Disclosure Exemptions
3. [This paragraph is not reproduced in the observer notes.]

ISSUE 1: ADDITIONAL CRITERIA FOR THE DEFINITION OF DISCONTINUED OPERATIONS

Background

4. At its May 14, 2008 Board meeting, the FASB indicated its preference to amend the previously agreed definition of discontinued operations to include in the definition subsidiaries that meet the criteria to be classified as held for sale on acquisition.
5. The staff prepared a memorandum for both Boards to discuss at their respective June Board meetings, which included a recommendation to include in the definition of discontinued operations subsidiaries that meet the criteria to be classified as held for sale on acquisition.
6. At its June 18, 2008 Education Session, the FASB discussed an alternative that would include in the definition of discontinued operations all **components of an entity** that meet the criteria to be classified as held for sale on acquisition, rather than **subsidiaries** that meet the criteria to be classified as held for sale on acquisition. The FASB did not make a decision since the meeting was held as an Education Session.
7. At its June 2008 Board meeting, the IASB briefly discussed the alternative discussed at the FASB Education Session. IASB Board members had concerns about modifying the definition to include all components of an entity that meet the criteria to be classified as held for sale on acquisition as a discontinued operation. This was because the inclusion of subsidiaries that meet the criteria to be classified as held for sale on acquisition in the current definition of discontinued operations was considered to be an exception to the general principle in defining discontinued operations. The exception was considered necessary to provide relief from the practical implications of the requirement to consolidate such subsidiaries. IASB Board members felt that the proposed modification would broaden the exception to the previously agreed definition of a discontinued operation beyond what is currently in IFRS 5. The IASB did not make a decision but asked the staff to perform additional analysis related to the various alternatives for the definition of discontinued operations discussed by the Boards and to present this analysis at a future meeting.

8. [This sentence is not reproduced in the observer notes.] The FASB plans to discuss issues raised in the Agenda Papers for the June and July IASB Board meetings on July 23, 2008.

Alternatives Considered

9. The staff considered four alternatives for the additional criterion to meet the definition of discontinued operations when a component of an entity that either has been disposed of or is classified as held for sale, in addition to those components that are operating segments. The four alternatives are:

View A: All **components of an entity** that meet the criteria to be classified as held for sale on acquisition

View B: All **subsidiaries** (in their legal form) that meet the criteria to be classified as held for sale on acquisition

View C: All **businesses** (as that term is defined in IFRS 3 *Business Combinations* (as revised in 2007)) that meet the criteria to be classified as held for sale on acquisition

View D: No additional criteria, only an operating segment can meet the definition of a discontinued operation

(Whether the disposal needs to be required by law or regulation in order to be classified as a discontinued operation is discussed later in this memorandum.)

View A: All Components of an Entity that Meet the Criteria to be Classified as Held for Sale on Acquisition

10. Proponents of View A believe it would be misleading to present profit or loss from components of an entity that meet the criteria to be classified as held for sale on acquisition in continuing operations because these components have not and will not be integrated in the entity. For instance, if these components were included in continuing operations of the entity, the profit or loss related to these components would be included in income from continuing operations of the current year but not for prior years (because they weren't held) and will cease to affect income from continuing operations within a year.

11. Since the definition of a component of an entity requires that operations and cash flows are clearly distinguished, operationally and for financial reporting purposes, from the rest of the entity, this proposed addition to the definition to discontinued operations would potentially prevent individual assets from being classified as discontinued operations. But the proposed addition would allow specific departments,

business lines, branches, subsidiaries and legal entities that meet the criteria to be classified as held for sale on acquisition to be included as discontinued operations. Proponents of View A believe that it is unnecessary to further narrow the criteria to a subsidiary or business to be classified as a discontinued operation and believe that to do so would only create complexity.

12. Proponents of View A acknowledge the inconsistency between the reporting of:

(1) components of an entity that meet the criteria to be classified as held for sale on Day 1 as discontinued operations and

(2) components of an entity that meet the criteria to be classified as held for sale on Day 2 and onwards as discontinued operations only if they meet other criteria

Nonetheless, proponents of View A believe that the costs of reporting all components of an entity that meet the criteria to be classified as held for sale on Day 1 in continuing operations would outweigh the limited benefits.

13. Opponents of View A believe that including all components of an entity that meet the criteria to be classified as held for sale on acquisition would change the general principle that has been developed for defining discontinued operations. The objective of reporting a discontinued operation is to distinguish disposal activities that reflect the strategic shift in an entity's business strategy, and the operating segment criterion with no exceptions would meet this objective. Expanding the definition to include all components of an entity that meet the criteria to be classified as held for sale on acquisition could potentially include disposed assets that do not necessarily reflect a strategic shift in the entity's business strategy.

View B: All Subsidiaries (in Their Legal Form) that Meet the Criteria to be Classified as Held for Sale on Acquisition

14. View B includes the same discussions as View A, except that proponents of View B believe that the component of an entity should be limited to subsidiaries (in their legal form) to be consistent with the current definition of a discontinued operation in IFRS 5. The definition in IFRS 5 includes 'subsidiaries acquired with a view to resale' (which, under the staff's interpretation, is equivalent to 'subsidiaries that meet the criteria to be classified as held for sale on acquisition'). The IASB included this exception in IFRS

5 to address cost-benefit concerns raised by constituents at the time it was issued. These proponents believe that there will be less disruption in practice if the definition continues to use the same criterion.

15. Proponents of View B also observe that a subsidiary would meet the criteria to be classified as held for sale on acquisition when, for example, (a) the subsidiary's business is unrelated to any of the existing segments or (b) the subsidiary is required to be disposed of by law or regulation (for example, because the entity would otherwise have too much of a concentration). Therefore, these proponents believe that reporting subsidiaries that meet the criteria to be classified as held for sale on acquisition as discontinued operations would be more consistent with the general principle to report discontinued operations, which is to distinguish disposal activities that reflect a strategic shift in the entity's business strategy, than to report all components of an entity that meet the criteria to be classified as held for sale on acquisition as discontinued operations.
16. Opponents of View B believe that the definition of discontinued operations should not refer to subsidiaries (in their legal form) because the legal form of the component of an entity should not be used as a criterion for determining whether and when a component is a discontinued operation. For example, whether a specific department or line of business (assuming it is not an operating segment) that meets the criteria to be classified as held for sale on acquisition is reported in discontinued operations would depend on whether it is in the legal form of a subsidiary.

View C: All Businesses (as that Term is Defined in IFRS 3 (as revised in 2008)) that Meet the Criteria to be Classified as Held for Sale on Acquisition

17. View C includes the same discussion as View B, except that it refers to a **business**, as defined in IFRS 3 (as revised in 2008) instead of a subsidiary (in its legal form). Proponents of View C believe that this alternative resolves some of the concerns raised by opponents of View B because it does not rely on the legal form of the component of an entity.
18. IFRS 3 (as revised in 2008) defines a **business** as 'an integrated set of activities and assets that is capable of being conducted and managed for the purpose of providing a return in the form of dividends, lower costs or other economic benefits directly to

investors or other owners, members or participants.’ Proponents of View C note that U.S. GAAP has the same definition of **business** in FASB Statement No. 141, *Business Combinations* (revised 2007) and, therefore, the Boards can have a common definition of discontinued operations if the term **business** were adopted.

View D: No Additional Criteria

19. Proponents of View D believe that adding criteria to the previously agreed definition of discontinued operations (which would include only operating segments that are disposed of or are classified as held for sale) would increase complexity and potentially undermine the objective of reporting discontinued operations. Since the determination of operating segments is based on how the chief operating decision maker makes decisions about allocating resources and assessing performance, disposal of an operating segment is likely to indicate the strategic shift in an entity’s business strategy and, therefore, reporting discontinued operations based on operating segments is likely to achieve the objective of this project. Proponents of View D also contend that all components of an entity (including subsidiaries and businesses) should be reported consistently, whether it meets the criteria to be classified as held for sale on acquisition (Day 1) or meets the criteria to be classified as held for sale on Day 2 or onwards.
20. Opponents of View D note that it would remove the relief from the practical implications of consolidation that was introduced by IFRS 5 at the time the exception from consolidation for subsidiaries acquired with a view to resale was removed from IAS 27 *Consolidated and Separate Financial Statements*. They contend that this project was never intended to reconsider that issue.

Staff Analysis and Recommendation

21. The staff supports View C for the following reasons:
 - (a) The staff is of the view that the operating segment criterion is the general principle that meets the objective of reporting discontinued operations. Any additional criteria should be considered an exception to the general principle.
 - (b) The staff believes an exception for certain components of an entity that meet the criteria to be classified as held for sale on acquisition should be included in the definition of discontinued operations to properly present trends in income from continuing operations. The staff is of the view that this exception will likely be limited in use since these components would need to meet the criteria to be

classified as disposal groups held for sale in accordance with IFRS 5 when they are acquired (that is, on Day 1).

- (c) The ‘subsidiaries acquired with a view to resale’ criterion in the current definition of discontinued operations in IFRS 5 was included to address cost-benefit concerns raised by constituents when IFRS 5 was issued. The staff is unaware of any changes in circumstances that suggest that this is no longer an issue and, accordingly, is of the view that a similar exception should continue to be provided. However, the staff shares the view that the reference to ‘subsidiaries’ focuses on the legal form of the component of an entity and should not be used as the criterion for determining whether and when a component is a discontinued operation. The staff believes that referring to a *business* (as defined in IFRS 3 (as revised in 2008)) would capture the substance without depending on the legal form.

22. Accordingly, the staff recommends that the Boards amend the previously agreed *definition* of discontinued operations so that it includes **businesses** (as defined in IFRS 3 (as revised in 2008)) that meet the criteria to be classified as held for sale on acquisition (View C).

Questions for the Board

1. *Does the Board agree to amend the proposed definition of discontinued operations to include businesses (as defined in IFRS 3 (as revised in 2008)) that meet the criteria to be classified as held for sale on acquisition (View C)?*
2. *If the Board does not agree with the staff recommendation (View C), does the Board agree with View A, B or D?*

Disposals Required by Law or Regulation

23. If the Board decides on either View A, B, or C in Question 1 or 2, another question to be considered is whether there should be an additional requirement that a component of an entity, subsidiary, or business (depending on the View selected in Question 1 or 2) that meets the criteria to be classified as held for sale on acquisition should only be classified as a discontinued operation if the disposal is **required by law or regulation**. Proponents of this alternative believe that this additional requirement could provide discipline over what components are classified as discontinued operations and thus would avoid abuse.
24. Opponents of this alternative believe that, in some cases, it would be very difficult to determine what is required by law or regulation. These opponents contend that the

form of whether the disposal was imposed by law or regulation should not dictate the accounting and reporting of discontinued operations.

25. The staff shares the views of opponents of this alternative and, therefore, recommends that this additional requirement should not be included in the definition if View A, B or C is selected by the Board.

Question for the Board

3. ***If the Board selects View A, B or C in Question 1 or 2, does the Board agree that it should not include an additional requirement that would limit the component of an entity, subsidiary, or business that meets the criteria to be classified as held for sale on acquisition to be reported in discontinued operations only when it is required by law or regulation?***

26. Based on the staff recommendations above, the revised definition of discontinued operations would read as follows:

A discontinued operation is a component of an entity that:

- (a) meets the definition of an *operating segment* in accordance with IFRS 8 *Operating Segments*, and either has been disposed of or is classified as held for sale, or
- (b) is a *business* in accordance with IFRS 3 *Business Combinations* (as revised in 2008) that meets the criteria to be classified as held for sale on acquisition.

27. While this project is conducted as a joint project and the staff recommendation is to have a common definition of discontinued operations, the staff is aware that the Boards may reach different conclusions in Question 1 or 2 because of the differences in existing guidance. In such case, the staff recommends that the Boards proceed to issuing Exposure Drafts with their respective views, instead of attempting to eliminate the difference(s) before issuing them. The staff is of the view that the Boards have achieved substantial convergence by agreeing on the general principle of the definition of discontinued operations (that is, the operating segment criterion) and any difference(s) in the exceptions to that definition should be considered relatively minor.

Question for the Board

4. ***If the Boards reach different conclusions, does the Board agree to proceed to issue an Exposure Draft with its view (and the FASB with its view) before eliminating the difference(s)?***

ISSUE 2: DISCLOSURE EXEMPTIONS

Background

28. At its April 2008 Board meeting, the IASB agreed that the proposed disclosures should not be required for subsidiaries that meet the criteria to be classified as held for sale on acquisition in order to be consistent with the current disclosure exemptions in IFRS 5. At its May 14, 2008 Board meeting, the FASB did not make a decision but asked the staff to come back to the Board after considering the interactions with the disclosure requirements in Statement 141(R).
29. The staff prepared a memorandum for both Boards to discuss at their respective June Board meetings, which included a recommendation to provide disclosure exemptions to both discontinued operations requirements and business combinations requirements for subsidiaries that meet the criteria to be classified as held for sale on acquisition.
30. At its June 2008 Board meeting, the IASB did not make a decision on this issue because, as discussed earlier, it did not decide as to whether subsidiaries that meet the criteria to be classified as held for sale on acquisition should be included in the definition of discontinued operations. However, the Board generally agreed that if disclosure exemptions were to be provided for discontinued operations requirements, exemptions should also be provided for business combinations requirements that require similar information.
31. [This paragraph is not reproduced in the observer notes.]

Staff Analysis and Recommendation

32. As discussed earlier in this memorandum, the staff recommends that the definition of discontinued operations include **businesses** (as defined in IFRS 3 (as revised in 2008)) that meet the criteria to be classified as held for sale on acquisition. Consistent with this staff recommendation, the staff recommends that disclosure exemptions be provided for business that meet the criteria to be classified as held for sale on acquisition.
33. The staff recommends that the following disclosure items should not be required for businesses that meet the criteria to be classified as held for sale on acquisition:

For discontinued operations requirements:

- (1) An analysis of the single amount reported as discontinued operations on the face of the statement of comprehensive income (IFRS 5, paragraph 33(b))
- (2) Net cash flows attributable to the operating, investing, and financing activities of discontinued operations (IFRS 5, paragraph 33(c))
- (3) Major classes of assets and liabilities of a disposal group (IFRS 5, paragraph 39)
- (4) Major classes of income and expenses, including impairments, depreciation and amortisation (a new requirement)
- (5) Profit or loss attributable to the parent, if the component of an entity includes non-controlling interests (a new requirement)

For business combinations requirements:

- (6) For acquired receivables, (i) the fair value of the receivables; (ii) the gross contractual amounts receivable; and (iii) the best estimate at the acquisition date of the contractual cash flows not expected to be collected (IFRS 3 (as revised in 2008), paragraph B64(h))
- (7) The amounts recognised as of the acquisition date for each major classes of assets acquired and liabilities assumed (IFRS 3 (as revised in 2008), paragraph B64(i))
- (8) The amounts of revenues and profit or loss of the acquiree since the acquisition date included in the consolidated statement of comprehensive income for the reporting period (IFRS 3 (as revised in 2008), paragraph B64(q)(i))
- (9) The revenue and profit or loss of the combined entity for the current period as though the acquisition date for all business combinations that occurred during the year had been as of the beginning of the annual period (IFRS 3 (as revised in 2008), paragraph B64(q)(ii))

[Two sentences are not reproduced in the observer notes.]

Question for the Board

5. ***Does the Board agree that disclosure exemptions should be provided to businesses (as defined in IFRS 3 (as revised in 2008)) that meet the criteria to be classified as held for sale on acquisition?***
6. ***Does the Board agree with the exempted disclosure items in paragraph 33?***