NESTLÉ S.A.

HERMANN WIRZ
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INTERNATIONAL ACCOUNTING STANDARDS BOARD
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For the attention of Ms. Anne McGeachin, Project Manager

Vevey, 24 October 2003

EXPOSURE DRAFT ED 4 DISPOSAL OF NON-CURRENT ASSETS AND PRESENTATION OF DISCONTINUED OPERATIONS

Ladies and Gentlemen,

We welcome the decision of the Board to address the issue of the disposal of non-current assets and the presentation of discontinued operations because the measurement and presentation of these assets play an important role in determining and presenting sustainable balance sheet and income statement information of an entity. We also welcome the IASB's and FASB's efforts to achieve convergence on this important subject but we do not consider that issuing a future IFRS that takes over the requirements of FAS 144 is the correct route to follow. ED 4 mixes several different requirements such as the measurement of assets held for sale and the presentation of discontinued operations, which in our opinion would better fit in amendments of IAS 16, 36 and 35.

Our principal areas of concern are as follows:

- We consider that only idle assets held for sale should no longer be depreciated. If an asset held for sale continues to be utilised until its date of sale, stopping its depreciation overstates its profitability and consequently does not result in a fair presentation of the profit or loss of discontinued operations.
- Since discontinued operations are generally sold as a bundle, we consider that their disclosure on the face of the balance sheet and on the face of the income statement should be a net basis, which does not prevent disclosing such operations on a gross basis in the notes.

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- We disagree with ED 4 proposal of defining discontinued operations as "a component of an entity that either has been disposed of or is classified as held for sale". We consider that this definition will result in disclosing too many discontinued operations and result in too many restatements of the entitles' accounts that would confuse the users. Instead we recommend to enhance the existing IAS 35 definitions.

The attachment to this letter answers the specific questions of the exposure draft. Please do not hesitate to contact us should you require additional information.

We thank you for allowing us to comment on this exposure draft and for your attention to our comments.

Yours very truly,

N E S T L E S. A.

H. Wirz
Senior Vice President
Head of Group Accounting and Reporting

Encl.

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ED 4 - ANSWERS TO SPECIFIC QUESTIONS AND OTHER POINTS

Question 1 – Classification of non-current assets held for sale

We agree that the separate classification of assets held for sale is useful to the users. It is also useful to the preparers because entities need criteria for reporting their held for sale businesses separately when a decision to sell has been taken.

We do not agree with a different treatment for assets to be abandoned. In such a case, non recoverable assets should simply be impaired to zero. If assets are idle but are to be recovered through their sale then they meet the definition as held for sale.

We also disagree with a classification of assets held for sale that encompasses both single assets and disposal groups that are held for sale. We consider that assets held for sale under this standard encompass the following two categories of assets that have a different nature:

a) idle assets that are held for being sold or otherwise disposed of, and
b) continuing assets held for sale (for which specific disclosure requirements should apply for discontinued operations).

As explained in our answer to question 2, this classification impacts the measurement of assets held for sale.

We also believe that, instead of issuing a new IFRS that should cover different types of assets held for sale, the Board should treat the measurement and presentation of single assets held for sale in a revision of IAS 16 and/or 36 and the presentation of discontinued operations in a revision of IAS 35 (see b above). If the Board really wants to issue a new standard on assets held for sale, it should distinguish single assets and discontinued operations in its presentation and measurement requirements and make such standard compatible with IAS 36.

Question 2 – Measurement of non-current assets classified as held for sale

We disagree with the measurement requirements on grounds of the economic nature of assets held for sale.

We consider that only idle assets that have been retired from active use should cease to be depreciated. The situation of continuing assets held for sale is different. While they should be subject to an impairment test, because the decision to sell an asset triggers an impairment indicator[1] and an impairment test which may result in the recognition of an

[1] IAS 36 § 9 (f)

impairment loss[2], the fact that they may be reduced to their net selling price does not imply that such assets should cease to be depreciated.

Since continuing assets held for sale would operate until the date of sale, we consider that they will continue to be consumed until that date and they should consequently continue to be depreciated (or, if appropriate, amortised). A wrong and overstated picture of the results of such assets held for sale would also be given if they would not be depreciated, which is important in connection with the disclosure requirements regarding discontinued operations.

We also disagree with the fact that joint ventures or associates held for sale would cease to be proportionately or equity consolidated and be recorded at fair value less cost to sell. We consider that recording such entities at fair value less cost to sell would result in disclosing artificially high results of such entities. Also we consider it is inappropriate to change the accounting treatment of such entities while they continue to be subject to joint control or to significant influence until the date of their disposal.

Question 3 – Disposal groups

We consider that the creation of disposal groups is not necessary because the decision to sell a group of assets leads to the creation of a distinct cash generating unit. Therefore the requirements of IAS 36 should be applicable for the allocation of an impairment loss to that cash generating unit[3].

Question 4 – Newly acquired assets

We agree with the requirement of measuring non-current assets held for re-sale upon an acquisition at fair value less cost to sell (or net selling price). This requirement should apply to assets that are re-sold because the acquirer does not want to retain a non-strategic part of the acquired business or because the acquirer cannot retain some parts of the acquired business as a result of a regulatory authority decision. Therefore the reason for measuring assets held for re-sale at net selling price is that such assets are recoverable out of their sale (because their owner does not want or cannot retain them) and not the alignment of IAS 27 to ED4 as mentioned in BC 40.

Question 5 – Revalued assets

This question is not applicable to us since we carry our assets at historical cost.

Question 6 - Removal of the exemption from consolidation for subsidiaries acquire and held exclusively with a view to re-sale

While we appreciate that the consolidation of such subsidiaries could be justified in terms of the entity having control during the period through the disposal, we nevertheless consider that the current approach of IAS 27 is superior in terms of predicting future cash flows

[2] IAS 36 § 58
[3] IAS 36 § 88

because such units were never part of the continuing performance of the entity. Therefore it is inappropriate to consolidate them and immediately regard them as discontinued operations. Furthermore the conditions of the appendix § B2 should explicitly mention the case of regulatory authorities which may grant a re-sale deadline of more than one year as was proposed in the improvement project as a response to some commentators[4].

Question 7 – Presentation of non-current assets held for sale

We do not agree with the gross presentation assets and liabilities. We consider that such presentation is not consistent with the fact that such assets are going to be sold as a bundle. Since non-current assets held for sale are principally recoverable out of the cash flows from their sale, such assets should be presented net so that the users can immediately identify them. A net presentation would also be useful to the preparers for helping them to distinguish the assets held for sale from their core business when communicating with the users.

Another aspect that we would raise is confidentiality. When an entity decides to sell a subsidiary or a business, the negotiations are generally kept secret in the first phase. Therefore disclosing financial information about assets held for sale would benefit to the prospective buyers and be detrimental to the selling entity. We recommend to foresee an exemption clause for confidentiality providing that the assets would be disclosed separately only when a public announcement of the negotiations is made.

Question 8 – Classification of discontinued operations

We do not favour the changes in classification because, as mentioned in this question, ED 4 requirements would result in classifying too many more discontinuing operations than the current IAS 35. Restatements of comparative figures would thus occur almost every year and this would confuse the users.

Since a separate presentation of discontinued operations should improve the predictive value of financial statements, we propose to enhance IAS 35 existing definitions by stating that the "discontinuation of a major line of business or geographical area of operations[5]" corresponds, for example, to a division, a region or a global or regional brand and by clarifying that the discontinuation should refer to a strategic single co-ordinated plan (As IAS 35 § 5 mentions only a single co-ordinated plan, we believe that the term "strategic" emphasizes on the importance of the transaction). Moreover, the negative definitions of IAS 35 § 8 should be maintained because it is important that tactical decisions to withdraw products or group of products, closure of factories, shifting manufacture of products do not qualify as discontinued operations.

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[4] IASB Update, December 02, page 8

[5] IAS 35 § 2 (b)

Question 9 – Presentation of a discontinued operation

We consider that the income statement should not be overloaded with separate disclosures of discontinued operations and we recommend a separate line on the income statement with a disclosure in the annexe, which is also consistent with what is proposed in the performance reporting project and with our recommendation above concerning the balance sheet (please see above under question 7).

Other points

Scope

We disagree with the exclusion of goodwill, deferred tax assets, employee benefit assets and financial assets from the scope of the standard, which reveals the contradiction of ED 4 which mixes individual assets held for sale with disposal groups.

While it is correct to exclude goodwill, deferred taxes, financial assets and employee benefits from the treatment of individual assets held for sale, they should be included in discontinued operations when they are going to be disposed with other assets. Non-current liabilities should also be included in discontinued operations when they are going to be sold with non-current assets.

Assets under finance leases should be treated in the same way as property plant and equipment since they have the same nature from a substance over form point of view, thus they should be included both as individual assets held for sale and in disposal groups.

Terminology

We disagree with the expression "fair value less costs to sell" and we propose to stick to the IAS 36 terminology of net selling price".