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Our Ref IAS/ED4

International Accounting Standards Board
30 Cannon Street
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United Kingdom

For the attention of Anne McGeachin

28 October 2003

Dear Ms McGeachin

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

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

In our view, the IASB should not focus on convergence of non-2005 agenda items to the potential detriment, in timeliness and quality, of the IFRS required for 2005. Though we support global convergence, we do not believe that the Board should be seeking to push through this particular change for 2005 when it is still working to complete its improvements project and other essential changes to IFRS to which it has already committed for 2005. We therefore propose that the Board should defer the proposals in ED 4 and revisit them as part of its comprehensive income project.

Whilst we agree that convergence is an excellent aim, we believe the Board's target should be convergence to the best standards operational, not necessarily to an existing one simply because it is there. We question whether simply adopting existing US GAAP requirements would achieve convergence to the best standard operational in this area.

Our key concern regarding the specific proposals is that we believe that the criteria for classifying assets as held for sale are subjective and rely too much on management intent. We therefore propose that there should be some requirement for demonstrable commitment by the balance sheet date. We also believe that assets held for sale should continue to be depreciated whilst they are still being used.

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We support the inclusion of a requirement that a discontinued operation shall be a separate major line of business or geographical area. We believe that the frequent adjustments to comparative information that will arise under the Board's proposals would not aid transparency.

We respond in detail to the questions raised in the Exposure Draft in the appendix. If you would like us to amplify our comments, please contact April Mackenzie on +1 732 516 5585 or Robert Carroll on +44 (0) 870 991 2210.

Yours sincerely

Grant Thornton

GENERAL COMMENTS

Timing and approach of the Exposure Draft

We support the aim of global convergence of accounting standards. However, in our view this aim is at present secondary to that of issuing, and securing full endorsement by the European Union of, IFRS in time for their adoption in 2005, including the completion of the Board's projects on improvements to existing standards, financial instruments, business combinations (part I) and share-based payment. We do not consider the proposals in ED 4 to be an essential component of the suite of standards for 2005, particularly as the comprehensive income project is not included. We therefore propose that the Board should defer the proposals in ED 4 and revisit them as part of its comprehensive income project. As the Board has consulted on this proposal, we suggest that they retain the comments and take them into account in their work on that project.

The Board has acknowledged the pressure on 2005 adopters in developing its innovative mechanism of "provisional final" standards – specifically initiated to allow even a little more time for those planning 2005 adoption. Issuing ED 4 cuts right across the benefits that the Board may have provided in this way.

Further, the aim of the convergence project should be to converge to the best quality standards. We are not convinced that the Board should effectively adopt the recent US GAAP standard without allowing time for its effectiveness in practice to be assessed and for FASB, and its Emerging Issues Task Force, to consider whether any amendments or additional guidance might be desirable as part of the convergence process with IFRS. In this context, we observe that the EITF will shortly be discussing practical issues related to the equivalent US standard, SFAS 144, which adds weight to the argument not to incorporate this standard into IFRS at this time. The existing IAS 35 has operated satisfactorily for some time, in our view, and arguments have not been presented by the Board to support proposing its replacement by the recent US rules.

RESPONSES TO SPECIFIC QUESTIONS

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

The Exposure Draft proposes that non-current assets should be classified as assets held for sale if specified criteria are met. (See paragraphs 4 and 5 and Appendix B.) Assets so classified may be required to be measured differently (see question 2) and presented separately (see question 7) from other non-current assets.

Does the separate classification of non-current assets held for sale enable additional information to be provided to users? Do you agree with the classification being made? If not, why not?

We agree that the classification of non-current assets as held for sale enables additional information to be provided to users. We also agree in principle with the classification being made, though we have concerns regarding the detail. In particular, we believe that the criteria in Appendix B paragraph 1 are subjective and rely too much on management intent. They could be met without significant public indicators, and are thus at the mercy of management manipulation. Only the reference in B1 (f) to "unlikely that the plan will be withdrawn" has any sense of irreversibility. We propose that there should be some requirement for demonstrable commitment by the balance sheet date, for example a public announcement or other means of raising a valid expectation that the entity will go through with its disposal plan.

In addition, we believe that the underlying principles of the proposed standard are not set out clearly. We propose that paragraphs 4 and 5 should be merged as the bold paragraph because, for an asset to be classified as held for sale, both the requirement that its carrying amount will be recovered principally through sale and the requirement to satisfy the criteria in Appendix B must be met. If the principle is simply that an asset is held for sale if its carrying amount will be recovered principally through sale, this could be argued to cover many investment properties, which is clearly not the Board's intention.

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

The Exposure Draft proposes that non-current assets classified as held for sale should be measured at the lower of carrying amount and fair value less costs to sell. It also proposes that non-current assets classified as held for sale should not be depreciated. (See paragraphs 8-16.)

Is this measurement basis appropriate for non-current assets classified as held for sale? If not, why not?

We support the general principle that assets held for sale should be carried at the lower of carrying amount and fair value less costs to sell. However, while an asset is still being used, we believe that depreciation should continue to be charged. Under the Board's proposals, assets will be classified as held for sale when the carrying amount will be recovered *principally* through sale. The portion of the carrying amount that will be recovered through use prior to sale should, in our view, be treated as depreciation. Failure to charge depreciation whilst the asset is still being used could also distort the profile of earnings, especially where the disposal does not give rise to a discontinued operation.

Question 3 – Disposal groups

The Exposure Draft proposes that assets and liabilities that are to be disposed of together in a single transaction should be treated as a disposal group. The measurement basis proposed for non-current assets classified as held for sale would be applied to the group as a whole and any resulting impairment loss would reduce the carrying amount of the non-current assets in the disposal group. (See paragraph 3.)

Is this appropriate? If not, why not?

We concur with this proposal.

Question 4 – Newly acquired assets

The Exposure Draft proposes that newly acquired assets that meet the criteria to be classified as held for sale should be measured at fair value less costs to sell on initial recognition (see paragraph 9). It therefore proposes a consequential amendment to [draft] IFRS X *Business Combinations* (see paragraph C13 of Appendix C) so that non-current assets acquired as part of a business combination that meet the criteria to be classified as held for sale would be measured at fair value less costs to sell on initial recognition, rather than at fair value as currently required.

Is measurement at fair value less costs to sell on initial recognition appropriate? If not, why not?

We concur with this proposal.

Question 5 – Revalued assets

The Exposure Draft proposes that, for revalued assets, impairment losses arising from the write-down of assets (or disposal groups) to fair value less costs to sell (and subsequent gains) should be treated as revaluation decreases (and revaluation increases) in accordance with the standard under which the assets were revalued, except to the extent that the losses (or gains) arise from the recognition of costs to sell. Costs to sell and any subsequent changes in costs to sell are proposed to be recognised in the income statement. (See paragraphs B6-B8 of Appendix B.)

Is this appropriate? If not, why not?

We concur with this proposal.

Question 6 – Removal of the exemption from consolidation for subsidiaries acquired and held exclusively with a view to resale

The Exposure Draft proposes a consequential amendment to draft IAS 27 *Consolidated and Separate Financial Statements* to remove the exemption from consolidation for subsidiaries acquired and held exclusively with a view to resale. (See paragraph C3 of Appendix C and paragraphs BC39 and BC40 of the Basis for Conclusions.)

Is the removal of this exemption appropriate? If not, why not?

We concur with this proposal.

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

The Exposure Draft proposes that non-current assets classified as held for sale, and assets and liabilities in a disposal group classified as held for sale, should be presented separately in the balance sheet. The assets and liabilities of a disposal group classified

as held for sale should not be offset and presented as a single amount. (See paragraph 28.)

Is this presentation appropriate? If not, why not?

We concur with this proposal. However, it is not clear to us whether paragraph 28 requires that some disclosure is made on the face of the balance sheet, such as total non-current assets and total liabilities classified as held for sale, or whether all information and analysis may be presented in the notes to the accounts.

Question 8 – Classification as a discontinued operation

The Exposure Draft proposes that a discontinued operation should be a component of an entity that either has been disposed of, or is classified as held for sale, and:

(a) the operations and cash flows of that component have been, or will be, eliminated from the ongoing operations of the entity as a result of its disposal, and

(b) the entity will have no significant continuing involvement in that component after its disposal.

A component of an entity may be a cash-generating unit or any group of cash-generating units. (See paragraphs 22 and 23.)

These criteria could lead to relatively small units being classified as discontinued (subject to their materiality). Some entities may also regularly sell (and buy) operations that would be classified as discontinued operations, resulting in discontinued operations being presented every year. This, in turn, will lead to the comparatives being restated every year.

Do you agree that this is appropriate? Would you prefer an amendment to the criteria, for example adding a requirement adapted from IAS 35 *Discontinuing Operations* that a discontinued operation shall be a separate major line of business or geographical area of operations, even though this would not converge with SFAS 144 *Accounting for the Impairment or Disposal of Long-Lived Assets*. How important is convergence in your preference?

We support the inclusion of a requirement that a discontinued operation shall be a separate major line of business or geographical area. This would reduce the scope for management manipulation of what is in the discontinued category. We also believe that the frequent adjustments to comparative information that could arise under the Board's proposals would not aid transparency.

Whilst we agree that convergence is an excellent aim, we believe the Board's target should be convergence to the best standards operational, not necessarily to an existing one simply because it is there.

Are the other aspects of these criteria for classification as a discontinued operation (for example, the elimination of the operations and cash flows) appropriate? If not, what criteria would you suggest, and why?

If our proposal above that a requirement for a discontinued operation to be a separate major line of business is not adopted, we recommend that the Board should consider the inclusion of a criterion that if disposal proceeds are reinvested in similar operations, the disposal should not count as a discontinued operation. To illustrate the point, real estate companies routinely sell operations and invest the proceeds in other similar operations. Under the Board's proposals, such entities would be reporting discontinued operations every year, which would not, in our view, provide meaningful information to users of the financial statements.

We note that the EITF in the USA will shortly be deliberating the meaning of the term "significant continuing involvement" and we suggest that the Board should study carefully the outcome of that deliberation in finalising its standard. For example, it may be helpful for the Board to clarify their understanding of the meaning of this term in the Basis for Conclusions.

In other respects, we concur with this proposal.

Question 9 – Presentation of a discontinued operation

The Exposure Draft proposes that the revenue, expenses, pre-tax profit or loss of discontinued operations and any related tax expense should be presented separately on the face of the income statement. (See paragraph 24.) An alternative approach would be to present a single amount, profit after tax, for discontinued operations on the face of the income statement with a breakdown into the above components given in the notes.

Which approach do you prefer, and why?

We favour the alternative approach of a single amount for profit after tax, with analysis in the notes, as we believe that the main focus of the income statement should be on the continuing operations. Hence, to include large amounts of information on discontinued operations on the face of the income statement would detract from this focus.

OTHER COMMENTS

Closure of operations

Under paragraph 23 of the proposed standard, a discontinued operation is a component that either has been disposed of or is classified as held for sale. Paragraph 6 states that components of the entity that are abandoned are presented as discontinued operations at the date on which they cease to be used, which implies that they may not be classified as discontinued prior to that date. However, we note that the proposed standard makes no mention of closure of operations rather than sale and we suggest that this aspect should be addressed specifically, even if it is merely to clarify that abandonment includes closure.

On the assumption that abandonment includes closure of an operation, we believe it is inconsistent to treat an operation as discontinued as soon as it is classified as held for sale, which may be up to a year before the sale is completed, but treat a closed operation as discontinued only from the date of closure, even if the decision to close was taken and announced some months previously, in such a way as to give rise to valid expectations in those affected that closure would be carried out. In our view, given the subjectivity and scope for management manipulation referred to in our response to question 1 above, it is possible that an entity could be far more committed to a closure than to a sale but be able to classify the latter as discontinued far earlier and more at a time of managements choosing than the former.

We therefore propose that criteria should be included in the final standard along the lines of those relating to classification as held for sale (taking account of our comments above) to enable an entity to identify an operation as discontinued when it is demonstrably committed to abandonment or closure, not just when the abandonment or closure has occurred.

We believe that the principle set out in paragraph 21 of the proposed standard supports this proposal. We see little difference between abandonment and sale of assets, except that the sale proceeds in the former case are nil. Hence, we do not see why there should be a significant difference in accounting between the two.

Definition of discontinued operation

The definition of discontinued operation in Appendix A states that a discontinued operation is a *component* of an entity etc. It is not clear to us whether 'component of an entity' is intended to mean the same thing as 'operation' or whether component is a subset, ie only those operations that can be clearly distinguished, etc. Given that 'operation' is used in what appears to be a different context in the definition of disposal group, we suggest that the Board considers improving the consistency of terminology in the definitions.

Cumulative translation differences relating to discontinued operations

We note that there are issues relating to the interrelationship between the cumulative translation differences in reserves arising under IAS 21.17 and impairment reviews under IAS 36 and measurement of assets held for sale under the Board's current proposals. We observe that the EITF considered this issue under US GAAP in Abstract 01-5. We appreciate that the Board does not wish to address the recycling issue at this time (as noted in paragraph BC26 in the Basis for Conclusions). However, they should appreciate that this issue might give rise to practical problems if a standard based on ED 4 were to be issued at the present time.

Appendix B — classification of non-current asset or disposal group as held for sale

We question the usefulness of sub-paragraphs B2 (a) and B2 (b). In our view these are loose and undermine the strength of the criteria established in paragraph B1. In particular, we believe they raise questions as to whether basic criterion (d) in paragraph B1 would have been met in the first place.

Recognition of gains and losses at the time of sale

Paragraph 15 of the proposed standard states that gains and losses not previously recognised by the time of sale of a non-current asset shall be recognised at the date of sale. However, the thrust of the proposed standard is such that losses will generally be recognised prior to sale. Therefore, we suggest that the Board may wish to clarify that this requirement relates to the rare circumstances where losses have not previously been recognised. Moreover, we question whether this paragraph adds any value to the proposed standard.