acteo Association pour la participation des entreprises françaises à l'harmonisation comptable internationale

Mouvement des Entreprises de France MEDEF

Exposure-draft ED 4 Disposal of Non-Current Assets and Presentation of Discontinued Operations

Overview of Acteo's position

Acteo welcomes the convergence effort undertaken by the IASB. However we believe that no subject should be dealt with on a piecemeal basis. In our view, abandoned assets and operations should not be left aside if consistency is to be ensured. We would therefore recommend that the Board reopens the scope of the proposed standard, even if it should result in discrepancies between US Gaaps and IFRS to be maintained slightly longer and be resolved after 2005.

Acteo believes that financial statements reflecting management's intent help users better assess the entity future cash-flows. Acteo therefore supports a separate classification for assets held for sale as proposed in the exposure-draft.

However, Acteo does not support:

1 depreciation ceasing at the time the decision of sale is made,

2 present definition of a component qualifying for discontinued operations; the proposed definition does not properly refer to the unit's business or geographical significance.

In order to deal with our concerns and nonetheless reach convergence, we hope that our recommendations would be shared with the FASB in view of a positive common outcome.

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Question 1: **Classification of non-current assets held for sale**

Acteo's answer

We agree with the proposed separate classification for assets held for sale. We believe that reflecting management's intent most often brings additional useful information to users of financial statements, helping them to assess more precisely the timing and certainty of future cash-flows. Designating and presenting separate information for assets held for sale is, in our view, one of those cases where it is useful that management's intent be reflected.

We have reviewed the list of criteria that are displayed in Appendix B. In our view:

- the main criterion is that the sale be **highly probable** since on that probability relies the level of certainty to be ensured to users; in our opinion all others substantiate that probability;
- the circumstances that makes the sale highly probable can be summarised as follows:
  - management is committed to a plan to sell: criteria a), c),
  - management has the ability to sell: criteria b), e), f)

- **the timing of the sale is also a matter of significance** to the users of financial statements; we however believe that a sale can be highly probable although its outcome is expected to occur beyond a twelve month period and therefore do not support the condition as being a key criterion for the classification of an asset as held for sale. B2 adequately describe some of those circumstances. 12 months should not be any magical number, and circumstances where a sale is highly probable should not be viewed as exceptions. We would therefore recommend that:
  - an asset be classified as held for sale only when the timing of the sale can be reasonably estimated;
  - the sale be expected to be completed within twelve months, unless management indicates and explains the reasons for a longer term in the notes.

We also believe that key requirements should not be excluded from the main text of the standard. Appendix B is in our view central to the proposed standard.

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

Acteo's answer

We disagree with the proposed measurement of assets held for sale. We believe depreciation should not cease as long as the assets are kept in active use. Depreciation, in our view, is essential to keeping profitability reliably presented in the income statement. We believe that assets held for sale do not request to be valued differently from other assets and that IAS 16 and 36 requirements provide adequate measurement bases. We believe that the sale decision may have an impact on the useful life of the asset and that IAS 16 requirements deal with reflecting that impact adequately. We also believe that the sale decision is an indicator that the asset may be impaired and hence calls for an immediate impairment test.
To make the information fully useful to the user of financial statements we believe that the fair value less costs to sell (we believe that "net selling price" was a better wording) should be disclosed in the notes.

We agree with the dissenting views of two Board members who support ceasing depreciation only when an asset is withdrawn from active use.

Question 3: **Disposal groups**

Acteo's answer

We fully agree that assets and liabilities that are to be disposed of together in a single transaction be treated as a disposal group.
Our answer to question 2 above removes any difficulty in dealing with or without goodwill since we have recommended that no change be made in the application of both IAS 16 and IAS 36.

Question 4: **Newly acquired assets**

Acteo's answer

We welcome the consequential amendment proposed to the final IFRS dealing with Business Combinations as we had requested that management's intent be reflected in the valuation of assets acquired through a business combination.
In a business combination context, management will have no difficulty, within a short-time period in a range of three months, to make selling parts of the assets and liabilities acquired, either through management's or anti-trust authorities' decision, highly probable. The identification of the exact perimeter of those assets or disposal groups to be disposed may however require more time. Since an allocation period for the cost of acquisition has been defined and is limited to a twelve months period, we recommend that this delay be granted to management to precisely identify and value disposal groups of assets acquired in a business combination.
We agree with the three-month delay in all other circumstances.

Question 5: **Revalued assets**

Acteo's answer

Here again, our answer to question 2 solves the issue. IAS 16 and 36 provide, in our view, adequate valuation bases.

Question 6: **Removal of the exemption from consolidation for subsidiaries**

Acteo's answer

We agree with the removal of this exemption as we consider it consistent with the requirements of the standard.

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Question 7: **Presentation of non-current assets held for sale Acteo's answer**

We agree that non-current assets classified as held for sale should be presented separately on the balance sheet. We also agree that assets and liabilities included in a disposal group should not be offset and presented as a single amount.
We believe useful to recall that IAS 1 requests assets and liabilities to be divided into current and non-current assets and that whenever management has indicated that a sale would occur beyond twelve months after balance sheet date assets held for sale should be presented divided into two separate captions on the face of the balance sheet.

Question 8: **Classification as a discontinued operation**

Acteo's answer

We disagree with the proposed definition of a discontinued operation as fitting any component of the entity, either disposed of or classified as held for sale, since the criterion of being operationally and financially separable is not sufficiently descriptive of the significance of the disposal group in terms of business.
Indeed such a definition is close to the definition of a cash-generating unit.

Identifying discontinued operations is designed to enhance the income statement predictive value. Discontinued operations should therefore be defined as fitting significant changes in the operations perimeter, such as to influence the sensitivity of the entity to external economic segmental factors. Discontinued operations should result from strategic decisions only whereas disposal groups that fit the component definition may arise from rationalisation and cost-cutting decisions.
We therefore believe that a disposal group qualifies as discontinued operations only if it meets IAS 35 §2 b) criterion, that is if it "represents a separate major line of business or geographical area of operations".
Otherwise, separating income from discontinued 'operations would lose significance and relevance to the user of financial statements. Some operations would be considered as being discontinued quite frequently, if not in every single reporting period, resulting in a heavy burden of restatements of all previous periods presented (need that is stated clearly in Question 8 wording but that remains implicit in the standard itself) for the entity and a loss of relevance and understandability for the users of financial statements.

Beyond the definition of a component and the criteria set out for discontinued operations (§22 and 23), the illustrative examples and the basis for conclusions indicate that our concern is shared with the Board. Our disagreement may hence be more a wording problem than a technical issue. Indeed conclusions reached in examples 8 through 11 in the implementation guidance seem to be in line with our comments and views.
In example 8 b) or 10 b), for instance, the brands are not considered as a component of the entity because they are part of a larger cash generating product group. We however do not understand such a condition to be set out in the definition of a component of an entity. In that example, it seems that not only a product group but also product lines and brands do satisfy the condition that their "operations and cash-flows can be clearly distinguished, operationally and for financial reporting purposes, from the rest of the entity". It is however clear to us that the beauty care business is a "separate major line of business" for the entity whereas single product lines or brands in that line of business are not.

If the entire issue amounts to a wording problem, we recommend that the present IAS 35 wording be maintained as it does not raise any difficulty of application or of understanding.
We feel however very cautious as the basis for conclusions indicate that the definition of a component is larger than the criterion stated in IAS 35.
We therefore call for clarification and a greater consistency between the wording of the standard itself and the examples and basis for conclusions.

Question 9: **Presentation of a discontinued operation**

Acteo's answer

We prefer the alternative approach. A single amount, profit after tax, for discontinued operations on the face of the income statement ensures greater readability of the most relevant figures in terms of predictive value. The detailed information set out in the notes is fully adequate for the analyses that should be based thereon.