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Ms A McGeachin
Project Manager
International Accounting Standards Board
30 Cannon Street
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30th October 2003

Dear Ms McGeachin,

Comments on ED 4, Disposal of Non-current Assets and Presentation of Discontinued Operations

We welcome this opportunity to comment on the IASB's Exposure Draft on the disposal of non-current assets and the presentation of discontinued operations.

The appendix attached to this letter provide responses to the questions set out by the IASB in its invitation to comment. In particular, we would like to highlight the following issues which give us particular concern. These points are discussed in more detail in our responses to the questions.

- We consider that an asset should not be classified as held for sale unless it has been retired from active use. We would recommend that this be added to the criteria which must be satisfied before an asset can be classified as held for sale. If assets which are still in active use are permitted to be classified as held for sale we do not believe it appropriate that depreciation should cease on such assets. .

- We feel that the widening of the definition of discontinued operations to capture potentially many more disposals and planned disposals risks burdening the primary financial statements with constant restatements and separate disclosures which will significantly reduce their usefulness to the user. Presentation of an operation as a discontinued operation should be limited, as it is now, to situations where a significant component of the reporting entity's activities is being sold or terminated.

Please contact me if you would like to discuss further any points in this letter.

Yours sincerely,

Mr PF Blackburn
Corporate Financial Controller
GlaxoSmithKline plc

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 differently (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?

Response

We agree that the separate classification of non-current assets held for sale will provide additional information that is useful to users of the financial statements.

On a drafting point, we would recommend moving the criteria in paragraphs 4 and 5 of Appendix B to within the body of the Standard. The criteria in Appendix B are crucial to correct application of the draft Standard's requirements, and relevant to an understanding of the implications of all the measurement, presentation and disclosure requirements within it.

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?

Response

We agree that the lower of carrying amount and fair value less costs to sell is an appropriate basis for measuring non-current assets classified as held for sale.

However, we only partially agree with the proposal that assets classified as held for sale should not be depreciated. We agree that this is appropriate for assets which have been retired from active use prior to their disposal. Indeed, we would suggest that retirement from active use should be added to the criteria in Appendix B as a further condition for classification of an asset as held for sale. In our view, continuing use in the business is not compatible with the criterion in B1(b) that the asset is available for immediate sale. If this revision of the definition of assets held for sale were to be adopted, we would agree that depreciation on all assets held for sale should cease.

However, if an asset held for sale does continue to be used in the entity's operations, we believe that operating costs in the income statement should not be reduced simply because an asset has been classified as held for sale. In our view, where economic benefits continue to be derived from use of an asset, reported operating costs should continue to reflect a charge for its consumption:

- If the asset is still held at its carrying value, depreciation should continue as if the asset's expected useful life and residual value had not changed. This treatment will ensure that the cost of the entity's operating activities is not distorted by classification of an asset as held for sale. It will eventually result in recognition of a larger gain on disposal, but this would be disclosed separately from operating costs.

- If the asset or disposal group is measured at fair value less costs to sell, an impairment loss will be recognised in operating costs immediately. In this situation, we agree that depreciation should cease as measurement is now based on expected disposal proceeds. Remeasurement to current fair value at each reporting date will, in any case, ensure that any reduction in the asset's value due to it being "used up" in the business is charged to the income statement, albeit labelled as impairment rather than depreciation.

We would also like to comment on the treatment of losses recognised at the date of sale. Paragraph 14 of the draft IFRS states that the impairment loss (or any subsequent gain) recognised for a disposal group shall reduce (or increase) the carrying amount of the non-current assets in the group that are included in the draft IFRS's scope. Paragraph 15 further notes that a gain or loss not recognised by the time of the sale shall be recognised at the date of sale. It is not clear from this whether a loss recognised on the date of sale should be recorded in the income statement as an impairment loss (in operating costs) or as a disposal loss which, according to the current ED of revised IAS 1 (paragraph 76(d)), should be disclosed on a separate line on the face of the income statement along with disposal gains. Conceptually it seems appropriate that, for an asset measured at fair value less costs to sell, a loss on date of sale is simply a revision to the impairment loss to reflect information not known at the time the asset was last remeasured. Similarly, a loss arising on an asset held at carrying value represents an impairment loss that would have been recognised earlier (and the asset remeasured to fair value less costs to sell) had the relevant information been available. This interpretation would result in any loss arising on the date of sale being recognised in operating costs along with other impairment losses, whereas treating the loss as a disposal loss would allow entities to report the loss on a separate line, possibly below operating profit. In order to ensure consistency of treatment of such losses among different entities we would encourage the IASB to clarify its intention in the final Standard.

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 single 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?

Response

We agree that the grouping of assets and liabilities that are to be disposed of together in a single transaction is appropriate, as the fair value measurement of the group as a whole will reflect the commercial reality of the expected disposal.

However, we believe that greater clarity should be provided in the discussion of the draft IFRS's scope in paragraph 2. Although the paragraph excludes various types of assets from the draft IFRS, all of these assets are included in the draft IFRS's measurement and presentation requirements provided they fall within a disposal group which also contains an asset which is covered by the draft IFRS. A comment in paragraph 2 to the effect that no assets are excluded from a disposal group would help clarify the scope of the draft IFRS.

We also note the following technical inconsistency, but accept that its incidence is likely to be infrequent. A disposal group measured at fair value less costs to sell will include a mixture of assets which have been impaired as a result of the remeasurement on to this basis and assets which have not been so impaired because they fall outside the scope of the draft IFRS. We note that paragraph 11 requires the latter group of assets to be measured in accordance with other applicable IFRSs before the fair value less costs to sell of the disposal group is measured, and that these assets will therefore reflect any impairments identified on their normal measurement basis. In most cases this should result in all the assets in the disposal group being reasonably measured, but an anomaly could arise in the case of goodwill. Draft IAS 36 requires measurement of goodwill at the lower of cost and recoverable amount and defines recoverable amount as the higher of fair value less costs to sell and value in use. If the cash-generating unit to which the goodwill is allocated has a value in use which is higher than its disposal value, this could result in goodwill in a disposal group being measured at value in use regardless of its inclusion within a disposal group and of the draft IFRS's principle that fair value less costs to sell is the appropriate measure (where this is lower than carrying amount).

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?

Response

We agree that initial measurement of these assets at fair value less costs to sell is appropriate. If all the criteria for classification as an asset or disposal group held for sale are met, then it would be inappropriate to recognise the assets at full fair value and not reflect the fact that the expected economic benefits indicated by this value will only be achieved by incurring the expected costs to sell. We also believe that is it important to ensure consistency of measurement of assets based on their current classification as held for sale and regardless of how or when they were acquired.

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 values 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?

Response

GlaxoSmithKline's accounting policy is not to revalue assets, so we do not have strong views on this question. However, the approach appears reasonable.

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?

Response

We agree with the removal of the exemption. In the interests of consistency of presentation across all assets held for sale, we believe it is important that all assets and liabilities are consolidated in the same way. Furthermore, clarity of information is improved for the user of the financial statements if assets and liabilities are not aggregated within a net figure.

We note that a further consequential amendment may be required to IAS 39 which, as it stands, appears to be incompatible with IAS 27 as revised by ED 4. Paragraph 1(a) of draft IAS 39 currently states that "an entity shall apply this Standard to account for an interest in a subsidiary, associate, or joint venture that according to IAS 27, IAS 28, or IAS 31 is acquired and held exclusively with a view to its subsequent disposal within twelve months from its acquisition". No consequential amendments to IAS 39 are noted in Appendix C to ED 4, but it would appear that this paragraph in IAS 39 should be reworded. Also, the reference in paragraph 11 of IAS 27 to paragraph 13 (deleted as a consequential amendment in ED 4) should be removed.

On the subject of accounting for ownership interests in other entities, we believe that the consequential amendment to IAS 28 *Accounting for Investments in Associates* (paragraph C4) is not helpful. The amendment provides for investments in associates to be accounted for either under IAS 39 if "the investment is acquired and held exclusively with a view to its subsequent disposal within twelve months from acquisition" or under ED 4 if it is "classified as held for sale [under ED 4]". In our opinion, any investment in an associate that management is prepared to describe as "acquired and held exclusively with a view to its subsequent disposal within twelve months of the acquisition" should be deemed to meet the criteria for classification as held for sale under ED 4. We would recommend that the possibility of accounting for investments in associates under IAS 39 be removed.

The same arguments apply to the treatment of joint ventures (paragraphs 35 and 36A (as revised by ED 4) in IAS *31 Financial Reporting of Interests in Joint Ventures)*.

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?

Response

We would prefer to disclose just one figure on the face of the balance sheet which would represent the total net assets and liabilities held for sale either individually or in disposal groups, with a full analysis provided in the notes to the financial statements. We believe a clear distinction between assets and liabilities held for continuing use in the business and those held for sale is useful to the user of the financial statements, and that this is best achieved by combining all items held for sale in one balance sheet line.

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 operating 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?

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?

Response

We believe that this definition of a discontinued operation is too broad and will lead to an onerous burden of restatement and disclosure requirements which is not justified by improved quality of information. Continual restatements are likely to reduce the ease with which financial statements can be understood by the user. We believe that a restatement of prior year comparatives should be a relatively rare event which will signal to the user that a significant operation is being discontinued.

We would therefore much prefer a definition similar to the one currently in IAS 35 referred to in the above question. The UK's FRS 3 also defines discontinued operations at a level which we feel to be appropriate when it describes them as operations whose sale "has a material effect on the nature and focus of the entity's operations and represents a material reduction in the entity's operating facilities".

While we generally support the objective of convergence with US GAAP, we do not believe that this objective should be pursued to the detriment of the quality of financial information reported by entities which have adopted IFRSs.

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?

Response

If the IASB were to change the definition of discontinued operations in the draft IFRS so that only significant operations could be classified in this way (see our response to question 8 above), we would support the proposal in the ED regarding presentation of these operations.

However, if the definition remains such that relatively small units are classified as discontinued, we would regard the separation of the results of discontinued operations from those of continuing operations in a single amount as more appropriate. This would avoid the distraction of many disclosures on the face of the income statement for potentially minor disposals, and enhance the predictive value of the information given in respect of continuing operations. We do agree that a breakdown should be provided in the notes so that no information is lost by this approach.