Date

7 September 2004

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Sir David Tweedie
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Dear Sir David,

Re: Exposure Draft of Proposed Amendments to IFRS 3 – Combinations by Contract Alone or Involving Mutual Entities

FEE (Fédération des Experts Comptables Européens – European Federation of Accountants) is pleased to submit its comments on the IASB Exposure Draft of Proposed Amendments to IFRS 3 on Combinations by Contract Alone or Involving Mutual Entities.

FEE as a founding organisation of EFRAG has also contributed to the EFRAG consultation process by submitting our views on their preliminary comments. This response should be read in conjunction with the response submitted by EFRAG. Where we are in agreement with the EFRAG comments we refer to their comments, where we are in disagreement our own views are put forward.

We support EFRAG's comments on the Exposure Draft and generally support the objectives of this Exposure Draft. We support the objective to avoid applying the pooling of interest method or the superseded purchase accounting method until further guidance is developed on the application of the purchase method to those specific situations. We also note that IAS 22 is now withdrawn from IFRS, making it impossible to continue to apply it to combinations by contract alone or involving mutual entities. The need for a transitional method and guidance is founded. However we repeat our concerns expressed in our comment letter on ED 3. The proposed "modified purchase method" will not resolve the difficulties to identify the acquirer, in situation where it is not possible to do so. Combinations in which separate entities are brought together to form a reporting entity by contract alone without the obtaining of an ownership interest are situations where such problem may rise. We support EFRAG's view that there are merger situations where it is difficult to justify the purchase method, particularly in transactions covered by this Exposure Draft. An appropriate alternative method needs to be considered urgently. We encourage IASB to continue to work on another solution when the purchase method is not the most suitable method.

We have the following comments on the questions raised in the draft standard.

Question 1

The Exposure Draft proposes:

(a) to remove from IFRS 3 the scope exclusions for business combinations involving two or more mutual entities and business combinations in which separate entities are brought together to form a reporting entity by contract alone without the obtaining of an ownership interest.

(b) to require the acquirer to measure the cost of a business combination as:

(i) the aggregate of the following amounts when the combination is one in which the acquirer and acquiree are both mutual entities:

• the net fair value of the acquiree's identifiable assets, liabilities and contingent liabilities; and

• the fair value, at the date of exchange, of any assets given, liabilities incurred or assumed, or equity instruments issued by the acquirer in exchange for control of the acquiree.

Therefore, goodwill would be recognised in the accounting for such transactions only to the extent of any consideration given by the acquirer in exchange for control of the acquiree.

(ii) the net fair value of the acquiree's identifiable assets, liabilities and contingent liabilities when the combination is one in which separate entities or businesses are brought together to form a reporting entity by contract alone without the obtaining of an ownership interest. Therefore, no goodwill would arise in the accounting for such transactions.

Is this an appropriate solution to the accounting for such transactions until the Board develops guidance on applying the purchase method to such transactions as part of a subsequent phase of its Business Combinations project? If not, what other approach would you recommend as an interim solution to the accounting for such transactions, and why?

The proposal of the Board is to invent another version of the purchase method, involving no goodwill and no capitalisation of costs directly attributable to the combination. We support EFRAG's suggestion. As an interim solution to the accounting for those transactions, we prefer if the Board would integrate its proposals more closely with the existing IFRS 3 requirements. The purchase method according to IFRS 3 should be applicable in all cases except if it is not practicable to measure the cost of the acquisition reliably. In such case, for business combinations involving mutual entities or in which separate entities are brought together by contract alone, the modified purchase method as proposed in the ED should be applied.

We do not support the proposed new paragraph 31B as the requirement to recognise costs directly attributable to the combination is inconsistent with IFRS 3. We believe the treatment of acquisition costs should be identical for all acquisitions. Furthermore, the proposal of IASB to require the costs directly attributable to the combination to be expensed in the current period is not explained in the Basis for Conclusions. We recommend the Board to amend the new paragraph 31B.

<u>Question 2</u>

The Exposure Draft proposes that no amendments be made to the transitional and effective date requirements in IFRS 3. This would have the effects set out in paragraph 6(a)-(c) above on the accounting for business combinations in which the acquirer and acquiree are both mutual entities or in which separate entities or businesses are brought together to form a reporting entity by contract alone without the obtaining of an ownership interest.

Is this appropriate? If not, what transitional and effective date arrangements would you recommend for such business combinations, and why?

We share EFRAG's concerns on the transitional requirements proposed in the Exposure Draft. Conceptually, the introduction of amendments which have effective date prior to the date of publication is not acceptable for high quality standard setting. As a principle, the IASB should not backdate the application date of standards.

However, in this case, we consider appropriate to have the same transitional and effective date requirements than in IFRS 3 and we agree with IASB proposals in Question 2. It would have a limited effect for European companies not applying IFRS 1 in 2005.

We would be pleased to discuss any aspect of this letter with you.

Yours sincerely,

David Devlin
President