CL 106

The Actuarial Profession
making financial sense of the future

25 March 2003

Ms Annette Kimmitt
Senior Project Manager
International Accounting Standards Board
30 Cannon Street
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Dear Ms Kimmitt

EXPOSURE DRAFT 3 BUSINESS COMBINATIONS

The UK actuarial profession is pleased to comment on ED3. We set out below responses to the questions posed but would first like to make the following high level observations:

- We believe that pooling of interest accounting continues to be justifiable for a small minority of mergers. However, we do appreciate that permitting this option can lead to abuse and in the interests of securing international convergence we are prepared to support the compulsory application of acquisition accounting. We would be prepared to consider favourably a possible replacement for pooling of interest based on “fresh start” accounting, which we understand is to be considered as part of Phase II of the Business Combinations project.

- We can see some theoretical advantages in replacing compulsory amortisation with an annual goodwill impairment test. However, this is only on the basis that proper controls exist, such as apply in UK GAAP, to ensure that purchased goodwill is not supported by pre-existing internally generated goodwill when carrying out the impairment test. We do not believe that the proposed IAS 36 provides such controls. We also believe that on practical grounds a company should be permitted to elect to amortise goodwill.

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The answers to the detailed questions posed are as follows:

1. We believe that the scope of the IFRS is reasonable.

2. We are prepared to accept the abolition of the pooling of interest method. Alternatively, if retained it should be made subject to the controls imposed in UK GAAP which if correctly policed would remove most of the abuses to which the method was subject under the previous version of US GAAP.

3. We believe the guidance to cover reverse acquisitions is appropriate.

4. Yes this is appropriate if the pooling of interest method is abolished.

5. We support this change.

6. Yes we support the proposed allowance for contingent liabilities. We would go further and suggest that the basic standard for contingent liabilities should also be on a fair value approach. We would also support a fair value approach for contingent assets.

7. We agree with the proposed treatment of minority interests.

8. We agree that goodwill should be recognised as an asset initially. We do have concerns with the proposition that subsequent write downs should be limited to those required by an impairment test unless that test is applied to the purchased goodwill in isolation, ie the test allows for the value of pre-existing goodwill.

9. We agree that negative goodwill can be credited directly to the income statement where the negative goodwill reflects a favourable purchase. Where, however, the negative goodwill reflects expected future losses associated with the acquired business, then we believe a case could be made for amortising the impact into the income statement.

10. We have no strong views on this.

We note the comments in B15(h) regarding net assets and liabilities associated with employee benefit schemes. The second sentence may need amendment to ensure consistency with any revised IAS 19. The need for the final sentence of B15 (i) highlights, we believe, the unsatisfactory nature of the current IAS dealing with deferred tax.

We have sent a copy of this response to the UK Accounting Standards Board. We would tend to agree with their view that the proposals set out in ED3 do not represent an improvement in financial reporting for the UK and Republic of Ireland.

Yours sincerely

PW Wright

P W Wright
Chairman
Accounting Liaison Group