CL 108

4th April 2003

Sir David Tweedie
International Accounting Standards Board
30 Cannon Street
London EC4M 6XH
United Kingdom

Dear Sir David

ED 3 Business Combinations

The Accounting Committee of the Institute of Chartered Accountants in Ireland (AC) supports the work being undertaken by the IASB and welcomes the opportunity to offer its comments. AC's detailed answers to the questions contained in exposure draft ED 3 are set out on the following pages but AC would like to draw your attention to some specific areas of concern.

AC has responded separately to the proposed amendments to IAS 36 and IAS 38.

Specific Areas of Concern

Group reorganisations

The proposed IFRS excludes 'transactions under common control' from the scope of the standard. This is consistent with the previous IAS 22. However, AC believes that the exclusion is more important in the current document. While excluded from the scope, AC believes that most preparers would have had regard to the guidance in the previous IAS 22 and applied merger or acquisition accounting as appropriate in group reorganisation situations. If preparers have regard to the draft IFRS they will only have guidance on acquisition accounting.

AC believes that merger / pooling of interest accounting is the correct approach to adopt for most group reorganisations. That is those that involve a share for share exchange, no impact on ultimate shareholders and no impact on minority interest. Group reorganisations are a common feature of most groups and AC believes that the revised IFRS should provide some guidance in relation to them. AC does not believe that it is necessary to wait for phase II and fresh start accounting.

<u>Comments on ED 3 Business Combinations</u>

1. ***The ED proposes:***

(a) ***to exclude from the scope of the IFRS business combination in which separate entities or operations of entities are brought together to form a joint venture, and business combinations involving entities under common control (see proposed paragraphs 2 and 3 and paragraphs BC9-BC11 of the Basis for Conclusions).***

Are these scope exclusions appropriate? If not, why not?

AC agrees with the proposed scope exclusions, except that AC believes strongly that it is inappropriate to provide no guidance on internal group reorganisations. As stated in our covering letter, AC believes that the IFRS should provide guidance on group reorganisations. Given that internal reorganisations are in practice extremely common it is necessary to include guidance as to how these should be accounted for. The prohibition of merger accounting in the context of internal organisations represents a significant gap in accounting guidance given the exclusion of internal reorganisations from the scope of the IFRS.

(b) ***to include in the IFRS a definition of business combinations involving entities under common control, and additional guidance on identifying such transactions (see proposed paragraphs 9-12 and Appendix A, and paragraphs BC12-BC15 of the Basis for Conclusions).***

Are the definition and additional guidance helpful in identifying transactions within the scope exclusion? If not, what additional guidance would you suggest, and why?

The definition of business combinations involving entities under common control and additional guidance provided are helpful. However, please see our comment under 1(a) above regarding the need for guidance on group reorganisations.

2. ***The Exposure Draft proposes to eliminate the use of the pooling of interests method and require all business combinations within its scope to be accounted for by applying the purchase method (see proposed paragraphs 13-15 and paragraphs BC18-BC35 of the Basis for Conclusions).***

   Is this appropriate? If not, why not? If you believe the pooling of interests method should be applied to a particular class of transaction, what criteria should be used to distinguish those transactions from other business combinations, and why?

AC supports the proposed prohibition on pooling of interests or merger accounting in the interests of eliminating the potential for manipulation and in light of the relatively small number of genuine mergers in business combinations. AC believes that in the vast majority of cases it is possible to identify an acquirer and an acquired entity in business combinations.

AC accepts the proposed requirement to use acquisition accounting in the remaining limited circumstances where there is a genuine uniting of interests, where combining entities are more akin to partners. AC understands that the IASB will review alternatives to acquisition accounting (e.g., fresh start accounting) to deal with these circumstances in Phase II of the Business Combinations project.

However, AC anticipates significant difficulties with the absence of guidance on the pooling of interests method for internal reorganisations. If entities were to follow the guidance in the proposed IFRS, acquisition accounting would be applied to group reorganisations, including identification of an 'acquirer' and adoption of fair values for the net assets of the 'acquired'. This would be unlikely to result in the best presentation where the group reorganisation was on a share for share basis, resulted in no changes to the ultimate shareholders and did not impact on any minorities. AC recommends transitional provisions allowing merger accounting for internal group reorganisations. The appropriateness of the method for such transactions can be considered further in Phase II of the business combinations project.

3. ***Under IAS 22 Business Combinations, a business combination is accounted for as a reverse acquisition when an entity (the legal parent) obtains ownership of the equity of another entity (the legal subsidiary) but, as part of the exchange transaction, issues enough voting equity as consideration for control of the combined entity to pass to the owners of the legal subsidiary. In such circumstances, the legal subsidiary is deemed to be the acquirer. The Exposure Draft proposes:***

   (a) to modify the circumstances in which a business combination could be regarded as a reverse acquisition by clarifying that for all business combination effected through an exchange of equity interests, the acquirer is the combining entity that has the power to govern the financial and operating policies of the other entity (or entities) so as to obtain benefits from its (or their) activities. As a result, a reverse acquisition occurs when the legal subsidiary has the power to govern the financial and operating policies of the legal parent so as to obtain benefits from its activities (see proposed paragraph 21 and paragraphs BC37-BC41 of the Basis for Conclusions).

   Is this an appropriate description of the circumstances in which a business combination should be accounted for as a reverse acquisition? If not, under what circumstances, if any, should a business combination be accounted for as a reverse acquisition?

AC believes the description is appropriate.

(b) ***additional guidance on the accounting for reverse acquisitions (see proposed paragraphs B1-B14 of Appendix B).***

Is this additional guidance appropriate? If not, why not? Should any additional guidance be included? If so, what specific guidance should be added?

The additional guidance is appropriate. However, AC recommends that the guidance make it clear that 'issued equity' includes not only the nominal value of shares but also other permanent reserves such as share premium, capital redemption reserves, and all other reserves that are subject to capital maintenance provisions. In an unlimited company, it will be share capital and share premium only.

4. ***The Exposure Draft proposes that when a new entity is formed to issue equity instruments to effect a business combination, one of the combining entities that existed before the combination should be adjudged the acquirer on the evidence available (see proposed paragraph 22 and paragraphs BC42-BC46 of the Basis for Conclusions).***

   Is this appropriate? If not, why not?

AC supports this approach.

5. ***Under IAS 22, an acquirer must recognise as part of allocating the cost of a business combination a provision for terminating or reducing the activities of the acquiree (a 'restructuring provision') that was not a liability of the acquiree at the acquisition date, provided the acquirer has satisfied specified criteria. The Exposure Draft proposes that an acquirer should recognise a restructuring provision as part of allocating the cost of a business combination only when the acquiree has, at the acquisition date, an existing liability for restructuring recognised in accordance with IAS 37 Provisions, Contingent Liabilities and Contingent Assets (see proposed paragraph 40 and paragraphs BC55-BC66 of the Basis for Conclusions).***

   Is this appropriate? If not, what criteria should an acquirer be required to satisfy to recognise a restructuring provision that was not a liability of the acquiree as part of allocating the cost of a combination, and why?

AC believes this is an appropriate restriction on recognition of provisions for reorganisations at acquisition. This proposal is to be welcomed as a necessary constraint on manipulation of goodwill measurement and on potential manipulation of post-acquisition performance.

In fact, AC would like to see the requirements of paragraph 40 expanded to deal with provisions established by the acquiree within, say, the twelve months prior to the combination. Particularly in a friendly takeover, there can be a very grey area around at whose instigation a reorganisation is being recognised. AC believes that the proposed rule is the one that should apply and only where the provision is part of the acquiree's intention should it form part of the fair value exercise. However, as an anti abuse measure, AC believes that where such provisions are established by the acquiree within say twelve months of the acquisition date, they should be required to be disclosed as a separate line item in the table of assets and liabilities acquired.

6. ***The Exposure Draft proposes that an acquirer should recognize separately the acquiree's contingent liabilities at the acquisition date as part of allocating the cost of a business combination, provided their fair values can be measured reliably (see proposed paragraphs 36 and 45 and paragraphs BC80-BC85 of the Basis for Conclusions).***

   Is this appropriate? If not, why not?

Yes. AC supports this approach. AC also believes that contingent assets should be recognised on the same basis as contingent liabilities. In some cases the contingent asset may be related to the contingent liability and to recognise one without the other would be inappropriate. Provided that the normal measurement rules are applied (ie more prudent measurement for assets) AC believes that there should be symmetrical treatment of contingent assets and contingent liabilities. AC is concerned by the suggestion in BC85 that this issue is being deferred to Phase II – if phase II leads to a different conclusion the standard can be amended then.

7. ***IAS 22 includes a benchmark and an allowed alternative treatment for the initial measurement of the identifiable net assets acquired in a business combination, and therefore for the initial measurement of any minority interests. The Exposure Draft proposed requiring the acquiree's identifiable assets, liabilities and contingent liabilities recognised as part of allocating the cost to be measured initially by the acquirer at their fair values at the acquisition date. Therefore, any minority interest in the acquiree will be stated at the minority's proportion of the net fair values of those items. This proposal is consistent with the allowed alternative treatment in IAS 22 (see proposed paragraphs 35 and 39 and paragraphs BC88-BC95 of the Basis for Conclusions).***

   Is this appropriate? If not, how should the acquiree's identifiable assets, liabilities and contingent liabilities recognised as part of allocating the cost of a business combination be measured when there is a minority interest in the acquiree, and why?

AC supports the elimination of alternatives where possible. AC also supports the specific treatment proposed for measuring minority interests by reference to the fair values of the identifiable assets including contingent assets acquired and liabilities and contingent liabilities assumed is considered appropriate.

8. ***The Exposure Draft proposes that goodwill acquired in a business combination should be recognised as an asset and should not be amortised. Instead, it should be accounted for after initial recognition at cost less any accumulated impairment losses (see proposed paragraphs 50-54 and paragraphs BC96-BC108 of the Basis for Conclusions).***

   Do you agree that goodwill acquired in a business combination should be recognised as an asset? If not, how should it be accounted for initially, and why? Should goodwill be

accounted for after initial recognition at cost less any accumulated impairment losses? If not, how should it be accounted for after initial recognition, and why?

AC believes that goodwill acquired in a business combination should be recognised as an asset.

AC believes there are substantial practical problems with the proposal that all goodwill should be included at cost less accumulated impairment losses, in the absence of robust methods for measuring impairment. AC's concerns with regard to the robustness of the impairment reviews are highlighted in the response to IAS 36. While generally AC supports the elimination of alternatives, the following paragraph explains that a majority of the committee would support an amortisation alternative being retained in this instance.

While amortisation is a crude approach to dealing with changes in the carrying amount of goodwill, it is a practicable way of acknowledging that goodwill is a real asset on which resources of the entity were spent in anticipation of future benefits. AC would like to see the rebuttable presumption of a maximum useful life of 20 years included in the IFRS. The committee also believes that systematic amortisation of goodwill is a pragmatic, if not perfect approach to dealing with this asset. On cost versus benefit considerations, annual impairment for all goodwill recognised in accounts is unattractive. A majority felt that there should not be an absolute ban on having systematic amortisation over the useful life of the goodwill. This was caused by a combination of different concerns, primarily regarding the cost of carrying out such reviews for smaller entities or transactions, combined with concerns over the robustness of the methodology for carrying out the impairment testing.

9. In some business combinations, the acquirer's interest in the net fair value of the acquiree's identifiable assets, liabilities and contingent liabilities recognised as part of allocating the cost of the combination exceeds that cost. The Exposure Draft proposes that when such an excess exists, the acquirer should:

(a) reassess the identification and measurement of the acquiree's identifiable assets, liabilities and contingent liabilities and the measurement of the cost of the combination; and

(b) recognise immediately in profit or loss any excess remaining after that reassessment.

(See proposed paragraphs 55 and 56 and paragraphs BC109-BC120 of the Basis for Conclusions).

Is this treatment appropriate? If not, how should any such excess be accounted for, and why?

AC was divided on this issue but the proposed approach to measuring and recognising negative goodwill was supported by a narrow majority of the committee.

There was, however, a strong minority view that the P&L charge should be spread over time. This minority felt that if it were not possible to identify what period to spread the negative goodwill over, then the default position should be to charge the negative goodwill over the useful life of the non-monetary acquired assets.

10. The Exposure Draft proposes that:

(a) If the initial accounting for a business combination can be determined only provisionally by the end of the reporting period in which the combination occurs because either the fair values to be assigned to the acquiree's identifiable assets, liabilities or contingent liabilities or the cost of the combination can be determined only provisionally, the acquirer should account for the combination using those provisional values. Any adjustment to those values as a result of completing the initial accounting is to be recognised within twelve months of the acquisition date (see proposed paragraphs 60 and 61 and paragraphs BC123-BC 126 of the Basis for Conclusions).

Is twelve months from the acquisition date sufficient time for completing the accounting for a business combination? If not, what period would be sufficient, and why?

No. AC believes that twelve months after the **end of the first accounting period** in which the acquired entity has been consolidated, rather than twelve months **after the date of acquisition,** is needed to complete the accounting and related fair value exercise.

(b) with some exceptions carried forward as an interim measure from IAS 22, adjustments to the initial accounting for a business combination after that accounting is complete should be recognised only to correct an error (see proposed paragraphs 62 and 63 and paragraphs BC127-BC132 of the Basis for Conclusions).

Is this appropriate? If not, under what other circumstances should the initial accounting be amended after it is complete, and why

AC agrees that any subsequent changes to carrying amounts of assets and liabilities acquired should be reflected in post-acquisition performance, unless an error qualifying as a prior period adjustment is identified. Please see comment below on tax assets.

Other Comments

Tax asset treatment (para 64)

AC is unhappy with the inconsistent treatment of deferred tax assets (as set out in paragraph 64). It is not clear to the committee why in this instance alone, the carrying amount of goodwill should be reduced immediately and recognised through the profit and loss account. Under the proposed amendment above, the acquirer will have twelve months from the end of the accounting period in which the acquisition occurs to identify any benefit in the acquiree's tax assets; this is considered to be sufficient. AC realises that this is being reconsidered in the second phase but does not support the retention of a different treatment to other assets.

Contingent assets

AC believes that contingent assets should be explicitly dealt with in this IFRS. While accepting a need to exercise greater prudence in the recognition of contingent assets in a business combination, AC believes that there should be symmetry of treatment with contingent liabilities.

Disposal of activity

Termination of business effect should be dealt with in addition to dealing with treatment of goodwill on disposal a business.

Sundry item

The wording in paragraph 69 should be changed to include 'impracticable' rather than 'undue cost and delay'.

If you require any clarification or further details on any of the points raised in the response please contact the Secretary to the Committee, Alix Brebbia on +353 1 6377316 or at alix.brebbia@icai.ie .

Yours sincerely

Alix Brebbia
Secretary
Accounting Committee
Institute of Chartered Accountants in Ireland

4th April 2003

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Dear Sir David

Amendments to IAS 36 Impairment of Assets and IAS 38 Intangible Assets

The Accounting Committee of the Institute of Chartered Accountants in Ireland (AC) supports the work being undertaken by the IASB and welcomes the opportunity to offer its comments. AC's detailed answers to the questions contained in the proposed amendments to IAS 36 and IAS 38 are set out on the following pages but AC would like to draw your attention to some specific areas of concern.

Specific Areas of Concern

IAS 36 – Impairment of Intangible Assets

Look back provisions

The AC considered that there should be some form of 'look back' introduced in relation to the projections. The fact that there is now more emphasis placed on the cash flow projections makes it very important that they should be realistic estimates of actual cash flows. Where this is not the case and actual cash flows are less than expected, there should be a reassessment of the 'value-in-use' calculation. We would support a requirement that actual cash flows should be inserted into cash flow projections and if these do not support the values attributed to the cash generating unit, an adjustment should be made.

IAS 38 – Intangible Assets

Customer lists and other similar intangibles

In IAS 38, the AC has one major concern which needs to be addressed. This concerns a potential inconsistency in relation to customer lists and other similar intangibles.

Paragraph 7 of the standard defines an intangible asset as an *identifiable* non-monetary asset without physical substance. The same paragraph defines an asset as a *resource controlled* by an entity as a result of past events and from which *future economic benefits are expected* to flow to the entity. The combination of these two definitions means that for an intangible asset to exist there must be identifiability, control over a resource and existence of future economic benefit (see para 9). These characteristics are discussed in paragraphs 10 to 16 of the draft standard.

In particular paragraph 14 argues that because of a lack of control over future economic benefits, a 'skilled workforce' will not meet the definition of an intangible asset. Paragraph 15 applies the same logic to customer lists (and similar assets such as customer loyalty, market share, customer relationships, etc) and states that an entity usually has insufficient control over the economic benefits from these items for them to meet the definition of intangible assets.

The Standard goes on to state in paragraph 32: "Therefore, in accordance with this [draft] Standard and [draft] IFRS X, an acquirer recognises at the acquisition date separately from goodwill all of the acquiree's intangible assets, excluding assembled workforces, irrespective of whether those assets had been recognised in the acquiree's financial statements before the business combination."

Additionally, in appendix A, the first example given of an intangible asset is an acquired customer list.

This needs to be addressed. The wording in para 32 seems to imply that an 'assembled workforce' is an intangible asset – just not one that should be recognised and appendix A is clear that a customer list is an example of an intangible asset – even though para 15 says it does not meet the definition of one.

The IASB needs to consider whether it intends customer lists and similar items to be recognised as intangible assets when they are purchased separately or in a business combination. If it does so intend then it needs to consider the language used in paragraph 15.

It may be appropriate to reconsider the issue of control in relation to both customer lists and a workforce. AC fully accepts that there is not 'control' in the legal sense of control but there is some form of de facto control – at least for a short time. This is partly the inertia to change which exists in relation to customer lists and control over remuneration policies and working conditions in relation to the workforce. It does not seem unreasonable that in certain acquisitions both of these could be seen as valuable assets acquired by the acquirer. If they meet the definition of an intangible asset, there would certainly be probability of future benefit (otherwise the acquirer would not consider them a valuable asset) and the acquirer would be able to measure the 'fair value' to him as reliably as any other unique intangible.

Comments on IAS 36 Impairment of Assets

1. ***Are the proposals relating to the frequency of impairment testing intangible assets with indefinite useful lives and acquired goodwill appropriate (see proposed paragraphs 8 and 8A and paragraphs C6, C7 and C41 of the Basis for Conclusions)? If not, how often should such assets be tested for impairment, and why?***

The AC agrees with the Board's proposals in relation to the frequency of impairment testing of intangible assets with indefinite useful lives and acquired goodwill. However, we have reservations in relation to the timing of the proposed reviews.

The AC does not agree with the inconsistency of requiring an annual impairment review of intangible assets to be completed at the end of the period and allowing the annual impairment review of acquired goodwill to be completed at any time during the year as long as it is performed annually. It is difficult to understand the rationale for differentiating between the timing of the annual impairment review required in respect of intangible assets with an indefinite life and that required for acquired goodwill. We anticipate practical difficulties with these proposals as in many instances the acquired goodwill and an intangible asset with an indefinite life will be in the same cash generating unit and assessed on the same projected cash flows. We fully support the approach that goodwill can be measured at any time during the year, provided consideration is given to any additional indicators of impairment happening between the date of testing and the year end. We would also support adopting the same approach for cash generating units with intangible assets having an indefinite useful life.

Moreover, given the increased reliance which must now be placed on the impairment review to assess the appropriateness of the carrying value of goodwill and intangibles, the AC considers that in addition to the annual impairment test requirement as set out in the text of the draft standard (paragraph 8 and 8A) the text of paragraph C7 from the Basis for Conclusions ("An entity should also be required to test such assets for impairment whenever there is an indication of possible impairment") should be added to the draft IFRS itself. This will ensure that entities do not present a misleading picture where they are required to report quarterly or on a half year basis in the event that there is a significant impairment.

2. ***The Exposure Draft proposes that the recoverable amount of an intangible asset with an indefinite useful life should be measured, and impairment losses (and reversals of impairment losses) for such assets accounted for, in accordance with the requirements of IAS 36 for assets other than goodwill (see paragraphs C10-C11 of the Basis for Conclusions). Is this appropriate? If not, how should the recoverable amount be measured, and impairment losses (and reversals of impairment losses) be accounted for?***

AC agrees with the Board's proposals that the impairment tests for intangible assets should be the same as those for assets other than goodwill (i.e., consistent with other identifiable assets covered in IAS 36). As stated above we would support permitting the timing of the remeasurement to be the same as for goodwill – that is at any time during the year provided it was done consistently and whenever there was an indicator of impairment.

3. ***The Exposure Draft proposes additional guidance on measuring the value in use of an asset. Is this additional guidance appropriate? In particular:***

   (a) should an asset's value in use reflect the elements listed in proposed paragraph 25A? If not, which elements should be excluded or should any additional elements be included? Also, should an entity be permitted to reflect those elements either as adjustments to the future cash flows or adjustments to the discount rate (see proposed paragraph 26A and paragraphs C66 and C67 of the Basis for Conclusions)? If not, which approach should be required?

AC agrees with the proposed inclusion of the items included in paragraph 25A.

AC considers that it would be helpful to provide guidance on how condition 25 (d) ("the price for bearing the uncertainty inherent in the asset") can be estimated. This guidance should refer to considering the entity's weighted average cost of capital adjusted for risk factors relevant to the asset / cash generating unit when considering the adjustment to the risk free rate that may need to be made when calculating the discounted present value of future expected cash flows.

   (b) should the assumptions on which cash flow projections are based take into account both past actual cash flows and management's past ability to forecast cash flows accurately (see proposed paragraph 27(a)(ii) and paragraphs C66 and C67 of the Basis for Conclusions)? If not, why not?

AC agrees with the proposal that management's past ability to forecast cash flows accurately should be taken into consideration.

   (c) is the additional guidance in proposed Appendix B to [draft] IAS 36 on using present value techniques in measuring an asset's value in use appropriate? If not, why not? Is it sufficient? If not, what should be added?

Given the complexity of the area AC considers that the inclusion of Appendix B in the standard is appropriate.

4. ***The Exposure Draft proposes that for the purpose of impairment testing, acquired goodwill should be allocated to one or more cash-generating units.***

   (a) ***Should the allocation of goodwill to one or more cash-generating units result in the goodwill being tested for impairment at a level that is consistent with the lowest level at***

which management monitors the return on the investment in that goodwill, provided such monitoring is conducted at or below the segment level based on an entity's primary reporting format (see proposed paragraphs 73-77 and paragraphs C18-C20 of the Basis for Conclusions)? If not, at what level should the goodwill be tested for impairment, and why?

AC agrees that goodwill should be tested for impairment at "the lowest level at which management monitors the return on the investment".

(b) ***If an entity disposes of an operation within a cash-generating unit to which goodwill has been allocated, should the goodwill associated with that operation be included in the carrying amount of the operation when determining the gain or loss on disposal (see proposed paragraphs 81 and paragraphs C21-C23 of the Basis for Conclusions)? If not, why not? If so, should the amount of the goodwill be measured on the basis of the relative values of the operation disposed of and the portion of the unit retained or on some other basis****?*

AC agrees with the recommendations made but consider that the standard should refer to 'terminated' activities as well as activities disposed of. The same treatment should be adopted for goodwill relating to a terminated activity as to an activity that is sold

(c) ***If an entity reorganizes its reporting structure in a manner that changes the composition of one or more cash-generating units to which goodwill has been allocated, should the goodwill be reallocated to the units affected using a relative value approach (see proposed paragraph 82 and paragraphs C24 and C25 of the Basis for Conclusions)? If not, what approach should be used?***

AC supported the theory of reallocation. However, there was considerable debate about how practical this was in practice. Care must be taken that this does not impose an unrealistic burden on entities. We believe that this proposal needs to be extensively field tested to ensure that it is possible to carry out such reallocations.

5. The Exposure Draft proposes

(a) that the recoverable amount of a cash-generating unit to which goodwill has been allocated should be measured as the higher of the unit's value in use and net selling price (see proposed paragraph 5 (definition of recoverable amount) and 85 and paragraph C17 of the Basis for Conclusions).

Is this appropriate? If not, how should the recoverable amount of the unit be measured?

(b) the use of a screening mechanism for identifying potential goodwill impairments, whereby goodwill allocated to a cash-generating unit would be identified as potentially

impaired only when the carrying amount of the unit exceeds its recoverable amount (see proposed paragraph 85 and paragraphs C42-C51 of the Basis for Conclusions).

Is this an appropriate method for identifying potential goodwill impairments? If not, what other method should be used?

(c) that if an entity identifies goodwill allocated to a cash-generating unit as potentially impaired, the amount of any impairment loss for that goodwill should be measured as the excess of the goodwill's carrying amount over its implied value measured in accordance with proposed paragraph 86 (see proposed paragraphs 85 and 86 and paragraphs C28-C40 of the Basis for Conclusions).

Is this an appropriate method for measuring impairment losses for goodwill? If not, what method should be used, and why?

AC agrees with the Board's proposals.

6. The Exposure Draft proposes that reversals of impairment losses recognised for goodwill should be prohibited (see proposed paragraph 123 and paragraphs C62-C65 of the Basis for Conclusions).

Is this appropriate? If not, what are the circumstances in which reversals of impairment losses for goodwill should be recognised?

AC agrees with the Board's proposals in this regard.

7. The Exposure Draft proposes requiring a variety of information to be disclosed for each segment, based on an entity's primary reporting format, that includes within its carrying amount goodwill or intangible assets with indefinite useful lives (see proposed paragraph 134 and paragraphs C69-C82 of the Basis for Conclusions).

(a) Should an entity be required to disclose each of the items in proposed paragraph 134? If not, which items should be removed from the disclosure requirements, and why?

(b) Should information to be disclosed under proposed paragraph 134 be disclosed separately for a cash-generating unit within a segment when one or more of the criteria in proposed paragraph 137 are satisfied? If not, why not?

The AC considers that requirement in 134 (d) is not appropriate as it would tend to give a spurious accuracy to the present value calculations. What is much more relevant is the sensitivity of the measurement to changes in assumptions and growth rates (ie 134 (e) (iv) and (v)).

Some concerns were expressed that the amount of information was too much and that important disclosures could be lost in the extent of detail. However, the counter argument to this is that in different circumstances, different parts of the disclosures could be more important than others and on balance it was considered that apart from 134 (d) all the other information should be provided.

Other Comments

The AC considered that there should be some form of 'look back' introduced in relation to the projections. The fact that there is now more emphasis placed on the cash flow projections makes it very important that they should be realistic estimates of actual cash flows. Where this is not the case and actual cash flows are less than expected, there should be a reassessment of the 'value-in-use' calculation. We would support a requirement that actual cash flows should be inserted into cash flow projections and if these do not support the values attributed to the cash generating unit, an adjustment should be made.

Comments on IAS 38

1. ***The Exposure Draft proposes that an asset should be treated as meeting the identifiability criterion in the definition of an intangible asset when it is separable or arises from contractual or other legal rights (see proposed paragraphs 10 and 11 and paragraphs B6-B10 of the Basis for Conclusions.***

   Are the separability and contractual/other legal rights criteria appropriate for determining whether an asset meets the identifiability criterion in the definition of an intangible asset? If not, what criteria are appropriate, and why?

The AC agrees with the Board's proposal that identifiability is the characteristic that conceptually distinguishes other intangible assets from goodwill.

The AC agrees with the Board's decision in relation to separability and contractual/other legal rights criteria and accepts that not being able to meet the criterion of separability in itself does not prohibit recognition as an intangible asset.

2. ***This Exposure Draft proposes clarifying that for an intangible asset acquired in a business combination, the probability recognition criterion will always be satisfied and, with the exception of an assembled workforce, sufficient information should always exist to measure its fair value reliably (see proposed paragraphs 29-32 and paragraphs B11-B15 of the Basis for Conclusions). Therefore, as proposed in ED 3, an Exposure Draft of a proposed International Financial Reporting Standard Business Combinations, an acquirer should recognise, at the acquisition date and separately from goodwill, all of the acquiree's***

intangible assets, excluding an assembled workforce, that meet the definition of an intangible asset (see proposed paragraphs 36, 43 and 44 of ED 3).

Do you agree that, with the exception of an assembled workforce, sufficient information can reasonably be expected to exist to measure reliably the fair value of an intangible asset acquired in a business combination? If not, why not? The Board would appreciate respondents outlining the specific circumstances in which the fair value of an intangible asset acquired in a business combination could not be measured reliably.

Subject to our concerns regarding the definition of an intangible asset and its application in the standard to workforces and customer lists (see Specific Areas of Concern above), etc, AC agrees that an acquirer should recognise all intangible assets in the acquiree. AC also considers that the acquirer will have sufficient information to measure them reliably at their best estimate. In fact, AC believes that in many cases the acquirer will have attributed a portion of the acquisition cost to the intangibles being acquired in arriving at its agreed acquisition cost.

The argument in paragraph 31 that the reason for not recognising a skilled workforce as an intangible asset (assuming it meets the definition) is purely due to inability to measure with sufficient reliability seems a rather large assumption. In some industries, the inherent skill and knowledge of the workforce may by the principle 'asset' acquired. AC believes that in general an acquirer can estimate with reasonable accuracy the portion of the acquisition price paid for an assembled workforce and to prohibit on this basis it's recognition as an asset is not justified

3. ***The Exposure Draft proposes to remove from IAS 38 the rebuttable presumption that an intangible asset's useful life cannot exceed twenty years, and to require its useful life to be regarded as indefinite when, based on an analysis of all of the relevant factors, there is no foreseeable limit on the period of time over which the asset is expected to generate net cash inflows for the entity (see proposed paragraphs 85-88 and paragraphs B29-B32 of the Basis for Conclusions).***

Is this appropriate? If not, under what circumstances, if any, should an intangible asset be regarded as having an indefinite useful life?

We agree with the revised proposals.

4. ***The Exposure Draft proposes that if an intangible asset arises from contractual or other legal rights that are conveyed for a limited term that can be renewed, the useful life shall include the renewal period(s) only if there is evidence to support renewal by the entity without significant cost (see proposed paragraphs 91 and 92 and paragraphs B33-B35 of the Basis for Conclusions).***

Is this an appropriate basis for determining the useful life of an intangible asset arising from contractual or other legal rights that are conveyed for a limited term that can be renewed? If not, under what circumstances should the useful life include the renewal period(s)?

There was some discussion as to whether the requirement as stated here was for some 'positive evidence' that renewal would happen or was it merely that there was 'no positive evidence' that it would not be renewed. Various members of the committee thought it meant one or other of these. The wording should be tightened to require positive evidence that renewal would happen before a renewal period should be treated as part of the useful life

5. ***The Exposure Draft proposes that an intangible asset with an indefinite life should not be amortised (see proposed paragraphs 103 and 104 and paragraphs B36-B38 of the Basis for Conclusions).***

   Is this appropriate? If not, how should such assets be accounted for after their initial recognition.

AC supports the non-amortisation of intangible assets with indefinite useful lives. However, as outlined in our response to IAS 36, we have some concerns in relation to the subjectivity of projected cash flows and the application of robust impairment reviews in practice. We recommend some form of 'look back' provision be introduced to assess the appropriateness of the projected cash flows. We also recommend that management or the board should approve the cash flows on which reliance is being placed

If you require any clarification or further details on any of the points raised in the response please contact the Secretary to the Committee, Alix Brebbia on +353 1 6377316 or at alix.brebbia@icai.ie .

Yours sincerely

Alix Brebbia
Secretary
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