Mr. Alan Texeira Senior Project Manager International Accounting Standards Board 30 Cannon Street London EC4M 6XH UK Letter of Comment No: 253 File Reference: 1204-001

Transmitted by email to: CommentLetters@iasb.org

Zurich, October 15th 2005

Comment of Swiss GAAP FER to Exposure Draft of Proposed Amendments to IFRS 3 Business Combinations, Comments to be received by 28 October 2005

Dear Mr. Alan Teixeira

The Swiss Accounting Standards Board (Swiss GAAP FER) is grateful for the opportunity to comment on the Exposure Draft (ED) above.

# 1. Overall Comments

Swiss GAAP FER is concerned about the Exposure Draft. The judgement is expanded and the proceedings are more complex.

Swiss GAAP FER regrets that in such a short time after Business Combination Phase I key issues as the purchase method have already been changed.

As mentioned in our comment to ED of proposed amendments to IAS 37 we think that there is a change in the measuring concepts. Therefore the IAS Framework

should first be amended, the Framework being the link between existing and new standards.

Swiss GAAP FER cannot support the full goodwill method. The full goodwill method will represent an additional accounting technique which encourages acquisitions (as e.g. the already implemented impairment-only approach). We all know that accounting should not influence business decisions. Full goodwill method will allow entities to recognise in the balance sheet original goodwill, e.g. goodwill for which no consideration had to be transferred.

Swiss GAAP FER does not agree that the consideration transferred (cost) is not necessarily the fair value of the interest acquired. This means breaking a taboo: To this day the cost of goods purchased was the benchmark for the fair value at the acquisition date. For good reasons: When purchasing an asset one is concerned that one should get at least as much value as one pays out. In our opinion this remnant of prudence should not be omitted. At least, what one pays is a backed-up market price. In a fair value differing from the acquisition price at the date of acquisition, a high degree of judgement and of subjectivity would be involved. In contrast, the purchase price at the date of acquisition is an impartial information. Paragraph 8 of the FASB ED of Proposed Statement of Financial Accounting Standards Fair Value Measurements of June 23rd 2004 says: "Valuation techniques used to estimate fair value shall be consistently applied". This should not be an issue at the acquisition date. Neither the Fair Value Measurement ED of FASB (Examples 6 to 8) nor the ED 3 IFRS (Examples 4 to 6) provide guidance of how estimates of the fair value at the acquisition date of a business as a whole are made. In the FASB ED the examples presented are in regard to single assets; and in the examples of ED IFRS 3 the fair value estimate of a business as a whole at the acquisition date is a provided information.

We have a feeling that the main issue of ED IFRS 3 is to achieve convergence with FASB which is certainly a valid approach. Swiss GAAP FER though gives a higher priority to the reliability and relevance of the financial statements. Moreover we think that convergence is a balanced procedure.

# 2. Comments relating to the questions asked

# Question 1 Objective, definition and scope

Are the objective and the definition of a business combination appropriate for accounting for all business combinations? If not, for which business combinations are they not appropriate, why would you make an exception, and what alternative do you suggest?

As outlined in the introduction to question 1 you want to know if the fair value measurement regardless of the percentage of the equity interests the acquirer holds in the acquiree at the acquisition date - is an adequate concept. No, we do not think so, as outlined above. Fundamental concept changes would have to be positioned first in the Framework. But we are, as a matter of principle, against the developed fair

value concept at the acquisition date. There is no need for a fair value concept with an escalated degree of judgement. The input measures in the case of an acquisition lack of market data. This is particularly so in the case of an illiquid market or a non-listed entity.

There are three implications that we reject in the fair value measurement concept of ED IFRS 3:

- 1. That the consideration transferred is not implicitly the fair value of the interest acquired
- That the fair value concept outlined in the ED implies the full goodwill method, eg that the goodwill of the minority interest is recognised in the balance sheet, and
- 3. The fair value concept in business combinations differs from the fair value concepts in other standards

We are concerned about the fair value concept implied by ED IFRS 3 the information of the financial statements will become less verifiable and less reliable.

# **Question 2 Definition of a business**

Are the definition of a business and the additional guidance appropriate and sufficient for determining whether the assets acquired and the liabilities assumed constitute a business? If not, how would you propose to modify or clarify the definition or additional guidance?

Yes, Swiss GAAP FER agrees with the definition of a business and the additional guidance.

# Questions 3 to 7 Measuring the fair value of the acquiree

# **Question 3**

In a business combination in which the acquirer holds less than 100 per cent of the equity interests of the acquiree at the acquisition date, is it appropriate to recognise 100 per cent of the acquisition-date fair value of the acquiree, including 100 per cent of the values of identifiable assets acquired, liabilities assumed and goodwill, which would include the goodwill attributable to the non-controlling interest? If not, what alternative do you propose and why?

As outlined under question 1, in a broader context, we do not agree that full goodwill method should be implemented. With the impairment-only concept the judgement has been increased. With a 100% goodwill recognised in the balanced sheet even if the interest acquired is, say 60 %, the decision whether a goodwill has to be impaired or not, develops an even higher impact.

# **Question 4**

The Exposure Draft proposes that a business combination is usually an arm's length transaction in which knowledgeable, unrelated willing parties are presumed to exchange equal values. In such transactions, the fair value of the consideration transferred by the acquirer on the acquisition date is the best evidence of the fair value of the acquirer's interest in the acquiree, in the absence of evidence to the contrary. Accordingly, in most business combinations, the fair value of the

consideration transferred by the acquirer would be used as the basis for measuring the acquisition-date fair value of the acquirer's interest in the acquiree. However, in some business combinations, either no consideration is transferred on the acquisition date or the evidence indicates that the consideration transferred is not the best basis for measuring the acquisition-date fair value of the acquirer's interest in the acquiree. In those business combinations, the acquirer would measure the acquisition-date fair value of its interest in the acquiree and the acquisition-date fair value of the acquiree using other valuation techniques. (See paragraphs 19, 20 and A8-A26, Appendix E and paragraphs BC52-BC89.)

Do paragraphs A8-A26 in conjunction with Appendix E provide sufficient guidance for measuring the fair value of an acquiree? If not, what additional guidance is needed?

As explained in the overall comment and in the answers to questions 1, we do not agree that for the few exceptions indicated we have to leave the technique to gross up the consideration transferred to get the fair value at the acquisition date of the business as a whole (and deduct the minority goodwill). You say in "most business combinations, the fair value of the consideration transferred by the acquirer would be used as a basis for measuring the acquisition-date fair value of the acquirer's interest in the acquiree". Swiss GAAP FER worries about the additional judgement allowed for, as you admit few possible cases.

# **Question 5**

Is the acquisition-date fair value of the consideration transferred in exchange for the acquirer's interest in the acquiree the best evidence of the fair value of that interest? If not, which forms of consideration should be measured on a date other than the acquisition date, when should they be measured, and why?

Yes, Swiss GAAP FER agrees.

#### **Question 6**

Is the accounting for contingent consideration after the acquisition date appropriate? If not, what alternative do you propose and why?

Yes, Swiss GAAP FER agrees.

# **Question 7**

Do you agree that the costs that the acquirer incurs in connection with a business combination are not assets and should be excluded from the measurement of the consideration transferred for the acquiree? If not, why?

Yes, Swiss GAAP FER agrees.

# Questions 8 and 9

Measuring and recognising the assets acquired and the liabilities assumed

## **Question 8**

Do you believe that these proposed changes to the accounting for business combinations are appropriate? If not, which changes do you believe are inappropriate, why, and what alternatives do you propose?

Yes, Swiss GAAP FER agrees.

# **Question 9**

Do you believe that these exceptions to the fair value measurement principle are appropriate? Are there any exceptions you would eliminate or add? If so, which ones and why?

Yes, Swiss GAAP FER agrees.

# Questions 10-12. Additional guidance for applying the acquisition method to particular types of business combinations

### **Question 10**

Is it appropriate for the acquirer to recognise in profit or loss any gain or loss on previously acquired non-controlling equity investments on the date it obtains control of the acquiree? If not, what alternative do you propose and why?

No comment of Swiss GAAP FER.

#### Question 11

Do you agree with the proposed accounting for business combinations in which the consideration transferred for the acquirer's interest in the acquiree is less than the fair value of that interest? If not, what alternative do you propose and why?

Yes, Swiss GAAP FER agrees.

# **Question 12**

Do you believe that there are circumstances in which the amount of an overpayment could be measured reliably at the acquisition date? If so, in what circumstances?

Swiss GAAP FER cannot think of such circumstances.

# Question 13 Measurement Period

Do you agree that comparative information for prior periods presented in financial statements should be adjusted for the effects of measurement period adjustments? If not, what alternative do you propose and why?

No comment of Swiss GAAP FER.

# Question 14 Assessing what is part of the exchange for the acquiree

Do you believe that the guidance provided is sufficient for making the assessment of whether any portion of the transaction price or any assets acquired and liabilities assumed or incurred are not part of the exchange for the acquiree? If not, what other guidance is needed?

No comment of Swiss GAAP FER.

# **Question 15 Disclosures**

Do you agree with the disclosure objectives and the minimum disclosure requirements? If not, how would you propose amending the objectives or what disclosure requirements would you propose adding or deleting, and why?

Swiss GAAP FER agrees basically with the disclosures required in ED IFRS 3, particularly in connection with the disclosures required by IAS 36. A possibility would be to amplify disclosures by requiring to show ranges of possible outcomes and sensitivity analyses. But we are not sure about this, since such disclosures could make the investors unnecessarily insecure.

# Questions 16-18 The IASB's and the FASB's convergence decisions

## **Question 16**

Do you believe that an intangible asset that is identifiable can always be measured with sufficient reliability to be recognised separately from goodwill? If not, why?

Swiss GAAP FER does not agree that, for the sake of convergence, the criterion that an intangible asset can be measured reliably if it is recognised in the balance sheet separate from goodwill, is eliminated.

Swiss GAAP FER does agree that the recognition of an assembled workforce acquired in a business combination as an intangible asset separate from goodwill is precluded.

# Question 17 to 19

Swiss GAAP FER agrees with the proposals made in ED IFRS 3.

We hope that you find the above comments helpful. If you wish to discuss them further, please do not hesitate to contact us.

Yours sincerely, Evelyn Teitler Member of the Board of Swiss GAAP FER