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Ms. Suzanne Bielstein  
Director, Major Projects and Technical Activities  
Financial Accounting Standards Board  
File Reference No. 1204-001  
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Dear Suzanne:

CIGNA Corporation appreciates the opportunity to share our views on the FASB Exposure Draft (ED), *Business Combinations - a replacement of FASB Statement No. 141*.

While we support the Board's intent, to provide pertinent and useful information to readers, we don't believe that the current proposal will have the intended effect. Of concern to CIGNA is the proposed treatment of transaction and restructure costs, pre-acquisition contingencies and contingent consideration. Specific to these areas, we believe the ED's guidance results in reporting that is unreliable and contrary to both existing authoritative literature and the underlying economics of a business combination.

In addition, we ask the Board to reconsider the provision that issuers retroactively restate for certain changes in estimate during the measurement period. We believe this requirement will confuse readers and is inconsistent with authoritative literature that requires changes in estimate to be reflected prospectively. Furthermore, we are concerned that the effective date of this ED, provided the final standard is issued in the fourth quarter of 2006, will not allow sufficient time for implementation.

Finally, we ask for clarification relative to the Board's definition of a business. It is currently unclear whether the ED would apply to certain reinsurance transactions that are common in the insurance industry. Our recommendations and key concerns are further discussed below.

Require capitalization of direct transaction costs

We believe that the process established to assign a value to the purchase of a business should be consistent with that followed to assign a value to the purchase of an individual asset. When an individual asset is acquired, its initial carrying value includes all direct costs incurred to put that asset in place. For example, today purchasers capitalize fees paid to survey a property (real estate acquisition), to compensate a broker/dealer (purchase an investment security) and to cover lease-related origination costs. Such costs are viewed as an unavoidable component of an acquirer's investment in that asset. Contrary to the argument of the Board in this ED, the costs of such services are considered by the acquirer to *contribute to the value* of the asset put in place and should be reflected as such.

It is our view that similar transactions should be accounted for similarly. Direct transaction costs incurred in connection with a business combination should be capitalized as part of the exchange because such costs are an unavoidable part of an acquirer's investment in that business and are considered by the acquirer to contribute to its value.

Require capitalization of exit costs contemplated at the time of acquisition

Consistent with the above discussion on transaction costs, we believe that restructure costs contemplated by an acquirer at the time of acquisition should be capitalized as part of the exchange provided management is committed to an exit plan and execution is imminent. Such costs are necessary to integrate and recognize synergies that contribute to the value of an acquired business and thus are a necessary cost of "putting the asset in place."

Permit valuation of preacquisition contingencies using recognition criteria provided in SFAS 5

We believe requiring fair value measurement for preacquisition contingencies will force companies to incorporate amounts in their financial statements that are not relevant or reliable, and could have unintended economic consequences. It is our view that the recognition, measurement and disclosure criteria outlined in Statement of Financial Accounting Standards (SFAS) No. 5, *Accounting for Contingencies* (SFAS 5) provide a rational and reliable basis for communicating with readers regarding contingent assets and liabilities. Therefore, we ask the Board to reconsider providing a valuation option using these criteria. Support for our argument against prescribing fair value measurement of preacquisition contingencies is as follows:

First, attempting to value contingencies where outcomes are exceedingly difficult to predict (as is the case with in-process litigation) will generate results that are misleading. Under this ED, acquiring companies will be required to record assets/liabilities that do not represent and may be materially different from the entity's ultimate cash benefit/obligation. Furthermore, measurements will be inconsistent. As significant judgment will be required to measure these contingencies using a cash flow model it

is inevitable that valuation will vary by issuer even when underlying facts and circumstances are similar. Finally, the result will be difficult to audit. As the assignment of probabilities to various scenarios is exceedingly subjective and will not be independently verifiable, the fair value requirement will pose a significant audit challenge.

Second, the subsequent revaluation requirement will introduce artificial and inappropriate volatility into the income statement. This increased volatility will mask earnings drivers and reported trends and increase the complexity of communicating with the investing public. If FASB insists that preacquisition contingencies should be measured and reflected in the basic financial statements at fair value, we ask the Board to reconsider the subsequent revaluation requirement and require remeasurement only upon occurrence of a triggering event.

Third, all aspects of the fair value requirement (disclosure, establishment of a liability and changes in subsequent value) could have a chilling effect on the marketability of some lines of business and could depress values. For instance, subjecting a litigation liability to this requirement would give an opposing party concrete information on an acquirer's assessment of the case and could compromise the acquirer's ability to economically settle or litigate. We believe it is important for FASB to consider the real economic effects of this requirement in its deliberations.

Finally, it is our view that measuring preacquisition contingencies at fair value regardless of whether they are "probable" of occurring will inappropriately result in disparate accounting within and across issuer financial statements. Under this ED, acquired contingencies will be valued differently from those that originated with the acquirer (currently accounted for under SFAS 5). We believe this inconsistent accounting is without basis and that contingencies that are similar in substance should be accounted for consistently under SFAS 5.

#### Permit SFAS 5 recognition criteria for contingent consideration

Also, we believe it is inappropriate to require upfront fair value measurement for contingent consideration if it is not probable it will be paid. To do so is inconsistent with the economics of the transaction. When contingent consideration is used in a business combination it is because parties cannot currently agree on the purchase price/ultimate value of the acquisition. As the two parties cannot agree on the business' current value, recognition of a fair value using probability factors is a subjective process that without doubt will produce two different values. Early recognition will not improve financial reporting as initial measurement will not reflect ultimate value. In addition, subsequent revaluation through net income will only undermine an entity's future operating earnings until the probability of payment is established. Furthermore, as indicated previously the subjectivity involved in assigning probabilities to various expected outcomes will prove challenging to audit.

If the Board continues to believe a fair value estimate of pre-acquisition contingencies is important to share with readers, disclosure is appropriate. This would provide for communication of estimated value to the readers

without inappropriately reporting unreliable measures in the basic financial statements and creating artificial earnings volatility. If FASB insists that contingent consideration be measured and reflected in the basic financial statements at fair value, we ask that FASB reconsider the subsequent revaluation requirement and require remeasurement only upon occurrence of a triggering event to minimize earnings volatility.

Prohibit retroactive restatement for changes in estimate during the measurement period

We believe, consistent with paragraph 19 of SFAS No. 154, *Accounting Changes and Error Corrections - a replacement of APB Opinion No. 20 and FASB Statement No. 3* that changes in estimate should be reflected prospectively and should not be accounted for by "restating or retrospectively adjusting amounts reported" or by "reporting proforma amounts" in current period financial statements. In addition to being inconsistent with existing literature, a restatement requirement would be unduly costly for issuers and further strain finance department resources. Furthermore, we believe this requirement could have unintended market consequences as the term "restatement" is most closely associated with accounting errors, and could be perceived negatively by investors, could potentially increase the risk of being required to report a material weakness under Sarbanes-Oxley and could generally decrease investor confidence in financial reporting.

Reconsider effective date

Given the significance of the changes proposed, we recommend that the effective date of the final standard be at least six months from its issue date. We believe this ED could be compared in terms of complexity to Statement of Financial Accounting Standards No. 123 (revised 2004), "Share-Based Payment" (SFAS 123R). The effective date of SFAS 123R, initially slated for six months after issue date, has since been delayed to provide for time for FASB to address unanticipated implementation issues and for preparers to modify internal reporting and control processes. We believe a similar transition period should be allowed for this equally complex ED.

Clarify applicability of guidance to reinsurance transactions of run-off blocks of business

In the normal course of business an insurance company may enter into reinsurance contracts to assume existing blocks of business from other insurance companies. Currently accounting for assumed blocks differs depending on whether the assumed business is considered to be "ongoing" (activities are expected to continue) or "in run-off" (only existing policies are to be renewed, no new policies will be written). Today, assumption of an ongoing block of business is generally treated as a business combination, while assumption of a run-off block is generally accounted for as a reinsurance transaction under SFAS No. 113, *Accounting and Reporting for Reinsurance of Short-Duration and Long-Duration Contracts*.

It is generally believed that the above noted treatment is consistent with the general concept of a business combination as outlined in SFAS No. 141 and Accounting Principles Board Opinion No. 16, both entitled *Business*

Technical Director

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*Combinations.* Furthermore, this treatment is supported by guidance provided by the SEC in Regulation S-X, Articles 3.05 and 11.01. These references to literature were grounded in the concept of "continuity." However, Appendix A, paragraph 6 of the current ED seems to suggest this accounting will no longer be appropriate. This paragraph specifically states, "...in evaluating whether a particular set is a business, it is not relevant whether the seller has operated the set as a business or whether the acquirer intends to operate the set as a business." We believe if the Board intends for "run-off" operations to be accounted for under business combinations guidance, the rationale should be addressed in the discussion points as this would be a significant departure from current practice.

If we can provide further information or clarification of our comments, please call me or Nancy Ruffino (860-226-4632).

Sincerely,

Anmarie Hagan