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Technical Director Financial Accounting Standards Board 401 Merritt 7 P.O. Box 5116 Norwalk, CT 06856-5116



LETTER OF COMMENT NO.

#### File reference: Proposed FSP FAS 144-d

PricewaterhouseCoopers LLP appreciates the opportunity to comment on the proposed FASB Staff Position No. FAS 144-d, *Amending the Criteria for Reporting a Discontinued Operation* (the "Proposed FSP").

We support the Board's efforts toward converging the discontinued operations criteria for US GAAP and IFRS. We have, however, certain concerns with the implications of the proposed amendments to the criteria for reporting a discontinued operation and the related disclosures. As further discussed below, our specific concerns with the proposals are as follows:

- We believe the level at which disposal activities are classified as discontinued operations may not be meaningful.
- We believe that the proposed disclosure requirements for disposals below the level an entity reports discontinued operations may be onerous, and
- We believe the costs of retrospective application will outweigh the benefits.

#### Definition of discontinued operation

We agree with the observations from users, described in the basis for conclusions, that disposal activities should be presented as discontinued operations only when an entity has made a strategic shift in its operations. However, restricting discontinued operations presentation to components that meet the definition of an operating segment, as that term is defined in FASB Statement No. 131, Disclosures about Segments of an Enterprise and Related Information (FAS 131), may not result in the presentation of disposals that represent a strategic shift in operations as discontinued operations. For example, the disposal of a component that represents a major geographical area that is not an operating segment would not qualify for presentation as a discontinued operation even though management may consider the disposal to be a strategic shift in operations. Further, an operating segment could include several key business activities that are reviewed together by a company's chief operating decision maker. A decision to dispose of one of these businesses may in fact, represent a strategic shift.

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The proposed definition may also result in the presentation of discontinued operations for some disposals of components that do not represent strategic shifts in operations. For example, some real estate investment trusts (REITs) may consider individual properties as separate operating segments. As proposed, a REIT that disposes of a single property may be required to present that property as a discontinued operation, even though its disposal may not represent a strategic shift in operations.

We believe that the definition of discontinued operations should allow companies the ability to apply judgment in their determination of whether a disposal activity represents a discontinued operation. In making that judgment, management should consider whether the entity has made a strategic shift in its operations. As such, we recommend that the FSP define a discontinued operation as a component of an entity that has been disposed of, or is held for sale, and for which disposal represents a strategic shift in operations.

If the definition is modified as per our recommendation, we also suggest that the FSP include the disposal of a component of a business that is reviewed regularly by management for the purpose of monitoring goodwill for impairment (i.e., a reporting unit) as an indicator of a strategic shift in operations. As noted in FASB Statement No. 142, *Goodwill and Other Intangible Assets* (FAS 142), a reporting unit constitutes a business for which discrete financial information is available and for which segment management regularly reviews operating results. Therefore, the level at which goodwill is tested for impairment reflects the way in which an entity manages its operations, even if such operations do not rise to a level of significance to be reviewed on a stand alone basis by the chief operating decision maker, as would be the case for operating segments defined by FAS 131. We believe consideration of disposals at the level at which goodwill is tested for impairment is consistent with the principle that discontinued operations should reflect strategic shifts in an entity's operations. Because disposals at the level at which goodwill is tested for impairment is only an indicator, companies will still be able to apply judgment in determining whether there has been a strategic shift in operations, even if there is no recorded goodwill.

While the frameworks for goodwill impairment testing are different under US GAAP and IFRS, the inclusion of the indicator we describe above would reduce complexity as it would incorporate existing guidance from International Accounting Standard 36, *Impairment of Assets* (IAS 36), and FAS 142 and harmonize goodwill impairment testing with the discontinued operations reporting under both US GAAP and IFRS. Determining the level at which goodwill is tested for impairment is generally well understood by preparers in the US and internationally.

As described in our response to Question 1 in the Appendix, if the Board elects not to change the definition of a discontinued operation as we have suggested, we believe the Board should consider retaining the foundation of the current IFRS definition with some improvements to establish a consistent framework of reporting and disclosure.

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### Disclosures and transition provisions

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We believe that the framework for disclosing disposal activities should be consistent with the framework for reporting discontinued operations. The disclosure requirements in the Proposed FSP may be onerous and may reflect disposals that are not strategic shifts in operations.

Lastly, we believe that retrospective application of the Proposed FSP may be challenging and not cost effective. We therefore recommend that the FSP be applied prospectively.

Our responses to the specific questions posed by the Board are included as an Appendix.

We appreciate the opportunity to express our views and would be pleased to discuss our comments or answer any questions you may have. Please contact Michael J. Gallagher (973-236-4328) or Larry Dodyk (973-236-7213) regarding our submission.

Sincerely,



**Appendix** 

### Proposed FASB Staff Position No. FAS 144-d, Amending the Criteria for Reporting a Discontinued Operation

Question 1: The proposed FSP would amend the definition of a discontinued operation so that a discontinued operation is a component of an entity that is (a) an operating segment (as that term is defined in FASB Statement No. 131, Disclosures about Segments of an Enterprise and Related Information) and either has been disposed of or is classified as held for sale or (b) a business (as that term is defined in FASB Statement No. 141 [revised 2007], Business Combinations) or a nonprofit activity that meets the criteria to be classified as held for sale on acquisition. Do you agree with the proposed definition of a discontinued operation? Why or why not? If not, what definition would you propose and why?

### PwC Response:

As discussed in our cover letter, we recommend that the definition of discontinued operations include all components of an entity that have been disposed or that are held for sale where the disposal represents a strategic shift in operations. Further, we believe the disposal of a component at which goodwill is tested for impairment should be an indicator of a strategic shift in operations and, therefore, a discontinued operation. This approach will provide companies with a framework for identifying discontinued operations and establish a level of consistency in application, as well as simplify the determination of which disposal activities should be presented as discontinued operations.

Determining the threshold for discontinued operations will continue to require judgment. For example, management may consider the disposal of a component representing a major geographical area to be a strategic shift in operations even though such component may not represent a reporting unit. Similarly, a REIT may determine that the disposal of an individual property that is considered an operating segment or reporting unit may not represent a strategic shift in operations.

In US GAAP, goodwill is tested for impairment at the reporting unit level. A component of an operating segment is required to be identified as a reporting unit if the component is a business for which discrete financial information is available and segment management regularly reviews the operating results. The reporting unit is the level of internal reporting that reflects the way an entity manages its business or operations.

In IFRS, goodwill is tested for impairment as part of a cash generating unit. Each unit or units to which goodwill is allocated must represent the lowest level at which goodwill is monitored for internal management purposes and must not be larger than an operating segment as defined by IFRS 8, *Operating Segments*. Applying the requirements in IAS 36 results in goodwill being tested for impairment at a level that reflects the way an entity manages its operations.

While the frameworks for goodwill impairment testing are different under US GAAP and IFRS, the level at which goodwill is tested for impairment under both frameworks is consistent in that it is at a level that reflects the way in which an entity manages its operations. Disposals at these levels are likely indicative of strategic shifts in an entity's operations that should be reflected as discontinued operations.

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**Appendix** 

Similar to the definition in the Proposed FSP, our suggestion would incorporate existing guidance around which there is already established practice. We believe that harmonizing the level for goodwill impairment testing with discontinued operations reporting would reduce complexity. Determining the level at which goodwill is tested is generally well understood by preparers of financial statements, both public and non-public, and appears to be more consistent with the principle that discontinued operations should reflect disposals that are strategic shifts in an entity's operations. Because disposals at the level at which goodwill is tested for impairment is only an indicator, companies will still be able to apply judgment in determining whether there has been a strategic shift in operations, even if there is no recorded goodwill.

Another alternative would be to retain the foundation of the current definition of discontinued operations in IFRS 5, *Discontinued Operations*, with some improvements. For example, we understand there is divergence in practice around whether the current definition includes only "major" geographical areas or "all" geographical areas. Such confusion should be clarified if the Board chooses this approach.

Question 2: Based on the proposed definition of a discontinued operation, an operating segment is the general level of aggregation for determining whether a component of an entity would be reported in the discontinued operation section of the income statement (or statement of activities for not-for-profit entities). The definition would no longer include certain subsidiaries and asset groups that do not meet the definition of an operating segment. Is it feasible for an entity that is not required to apply Statement 131 (that is, a nonpublic component of an entity and a not-for-profit entity) to determine whether the component of an entity meets the definition of an operating segment? Why or why not? If not, what definition would you propose for an entity that is not required to apply Statement 131 and why?

#### **PwC Response:**

Nonpublic companies are required to identify their operating segments as a first step in determining reporting units for purposes of goodwill impairment testing. As such, we believe it is feasible for an entity that is not required to apply FAS 131 to determine whether the component of an entity meets the definition of an operating segment. However, as discussed in our cover letter and in our response to Question 1, we would suggest a different approach.

**Question 3:** Do you agree with the proposed disclosure requirements? Why or why not? If not, what changes would you propose and why?

#### PwC Response:

We disagree with the proposed disclosure requirements. We believe the framework for disclosing disposal activities should be consistent with the framework for reporting discontinued operations. We agree with the observations from users described in the basis for conclusions that disposal activities should be presented as discontinued operations only when disposals represent strategic shifts in an entity's operations. We believe users would likely benefit from a level of disclosure for discontinued operations that mirrors the level of reporting in the primary set of financial statements.





Question 4: Under the disclosure requirements, income tax expense or benefit does not have to be calculated and disclosed for components of an entity that are reported within continuing operations and that have been disposed of or are classified as held for sale. Do you agree or do you believe it would be beneficial to require income tax expense or benefit to be calculated and disclosed for discontinued components of an entity within continuing operations? If so, how would you calculate and disclose the income tax expense or benefit?

#### **PwC Response:**

We agree with the Proposed FSP that income tax expense or benefit would not need to be calculated and disclosed for components of an entity that are reported in continuing operations and that have been disposed of or are classified as held for sale.

Question 5: Do you agree with the disclosure exemptions for a business or a nonprofit activity that meets the criteria to be classified as held for sale on acquisition? Why or why not? If not, what changes would you propose and why?

#### **PwC Response:**

We agree with the disclosure exceptions for a business or a nonprofit activity that meets the criteria to be classified as held for sale on acquisition.

**Question 6:** Are the effective date and transition provisions sufficient for compiling the information needed? Why or why not? If not, what would you propose and why?

#### PwC Response:

We believe that prospective application is appropriate. We believe that information necessary to carve-out the disposal of an operating segment that did not previously meet the definition of a discontinued operation (e.g., the conditions in paragraph 42 of FAS 144 had not been met) may be difficult to obtain and result in significant increased costs for the issuer as information prepared for internal management reporting may not be prepared in accordance with US GAAP.

Further, we note that FASB Statement No. 144, Accounting for the Impairment or Disposal of Long-Lived Assets, required prospective treatment upon initial adoption. In paragraph B130 of that Standard, the Board noted that "obtaining or developing the information necessary to apply this Statement retroactively could be burdensome for many entities...The Board concluded that prospective application for disposal transactions is the most reasonable and practical transition approach when considered together with the need for consistent transition provisions for disposal transactions and the cost associated with retroactive application." Similarly, we believe prospective application is appropriate for the FSP.