Dear Mr Teixeira

Proposed amendments to IFRS 3 “Business Combinations” and IAS 27 Consolidated and Separate Financial Statements”

We welcome this opportunity to comment on the proposals arising from the second phase of the IASB’s Business Combinations project.

We understand the conceptual approach that the fair value of the acquiree as a whole should be recognised in the consolidated balance sheet of the parent entity, and that this will entail recognition of 100 per cent of goodwill in any business combination in which the acquirer obtains control. However, as we note below, we have concerns over some aspects of how this could be implemented in practice, and over other issues addressed within the Exposure Drafts:

• We are concerned that the proposed measurement basis of goodwill will reduce the quality of financial information, as the fair value of the acquiree as a whole is considerably more difficult to measure reliably than the fair value of the consideration transferred. If this approach to measuring goodwill is to be adopted, we would request that more guidance be provided on valuation, and that this guidance be thoroughly validated, perhaps through discussion with preparers of financial statements and field testing of its application in real situations.

• We strongly oppose the proposal that remeasurement of contingent consideration should always result in gains and losses in the income statement. We believe that, in many cases, the remeasurement arises from the receipt of better information concerning the fair value of the acquiree at the acquisition date. These remeasurements do not relate to post-acquisition profits or losses, but should adjust the fair value recognised for the acquiree at acquisition date.
PROPOSED CHANGES TO IFRS 3 “BUSINESS COMBINATIONS”

Question 1—Objective, definition and scope

The proposed objective of the Exposure Draft is:

...that all business combinations be accounted for by applying the acquisition method. A business combination is a transaction or other event in which an acquirer obtains control of one or more businesses (the acquiree). In accordance with the acquisition method, the acquirer measures and recognises the acquiree, as a whole, and the assets acquired and liabilities assumed at their fair values as of the acquisition date. [paragraph 1]

The objective provides the basic elements of the acquisition method of accounting for a business combination (formerly called the purchase method) by describing:

(a) what is to be measured and recognised. An acquiring entity would measure and recognise the acquired business at its fair value, regardless of the percentage of the equity interests of the acquiree it holds at the acquisition date. That objective also provides the foundation for determining whether specific assets acquired or liabilities assumed are part of an acquiree and would be accounted for as part of the business combination.

(b) when to measure and recognise the acquiree. Recognition and measurement of a business combination would be as of the acquisition date, which is the date the acquirer obtains control of the acquiree.

(c) the measurement attribute as fair value, rather than as cost accumulation and allocation. The acquiree and the assets acquired and liabilities assumed would be measured at fair value as of the acquisition date, with limited exceptions. Consequently, the consideration transferred in exchange for the acquiree, including contingent consideration, would also be measured at fair value as of the acquisition date.

The objective and definition of a business combination would apply to all business combinations in the scope of the proposed IFRS, including business combinations:

(a) involving only mutual entities

(b) achieved by contract alone

(c) achieved in stages (commonly called step acquisitions) in which the acquirer holds less than 100 per cent of the equity interests in the acquiree

(d) at the acquisition date.

(See paragraphs 52-58 and paragraphs BC42-BC46 of the Basis for Conclusions.)

Question 1—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?

GSK Response

We agree with the objective and the definition. We believe that it is appropriate that the acquirer should measure and recognise the acquiree as a whole in acquisitions where less than 100 per cent of the acquiree is purchased, and that fair value, rather than cost accumulation and allocation, should be the measurement attribute. We support the recognition of the full value of goodwill as this aligns its
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treatment with that of other net assets acquired. However, while we can follow the conceptual arguments, we have reservations about some of the practical implications, such as the difficulty of measuring 100% of the goodwill of an entity when less than 100% of the entity has been acquired.

We are concerned that requiring acquirers to measure the fair value of the acquiree as a whole introduces further estimation and subjectivity into the measurement of goodwill, reducing the reliability of a balance which is already difficult to measure with certainty. Goodwill currently reflects any errors or uncertainty in measurement of the other assets or liabilities acquired, and includes items which are not recognised separately as they are not reliably measurable, for example an assembled workforce. Replacing the fair value of consideration transferred with the fair value of the acquiree as a whole in the “other side of the equation” will further reduce the reliability and information content of goodwill. We believe more guidance should be provided on the valuation of goodwill, supported by further research into the practical issues of valuing goodwill. Please see our response to Question 4 below for our more detailed comments on this point.

**Question 2—Definition of a business**

The Exposure Draft proposes to define a business as follows:

A business is an integrated set of activities and assets that is capable of being conducted and managed for the purpose of providing either:

(1) a return to investors, or

(2) dividends, lower costs, or other economic benefits directly and proportionately to owners, members, or participants. [paragraph 3(d)]

Paragraphs A2-A7 of Appendix A provide additional guidance for applying this definition. The proposed IFRS would amend the definition of a business in IFRS 3. (See paragraphs BC34-BC41.)

**Question 2—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?**

**GSK Response**

We agree that it is appropriate to widen the current definition of a business in IFRS 3 to include all sets of activities or assets which are capable of being conducted and managed to provide a return to investors or other economic benefits.

However, given the widening of the definition to cover possible uses as well as actual uses, we are concerned that there may be instances where it is not easy to decide whether a business has been acquired or just a group of net assets. It is unfortunate that the accounting treatment will continue to differ depending on this determination, and we regret that the Board’s preference, expressed in paragraph BC41, for expanding the scope of the proposed revised IFRS 3 to acquisitions of asset groups was not able to be achieved. As a consequence, the identification of an acquisition as a business or an asset group continues to have significant accounting implications, such as recognition or not of goodwill. It would therefore be helpful to preparers of financial statements if the Board were to include some examples in the Application Guidance to illustrate both situations.

**Questions 3-7—Measuring the fair value of the acquiree**

The Exposure Draft proposes that in a business combination that is an exchange of equal values, the acquirer should measure and recognise 100 per cent of the fair value of the acquiree as of the acquisition date. This applies even in business combinations in which the acquirer holds less than 100 per cent of the equity interests in the acquiree at that date. In those business combinations, the acquirer would measure and recognise the non-controlling interest as the sum of the non-controlling interest’s proportional interest in the acquisition-date values of the identifiable assets acquired and
liabilities assumed plus the goodwill attributable to the non-controlling interest. (See paragraphs 19, 58 and BC52-BC54.)

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?

GSK Response

We understand the conceptual arguments for treating goodwill in the same way as all other assets, ie recognition in full with the non-controlling interest being allocated its share. However, we believe that there are practical difficulties in applying the conceptual approach to real business combinations. In particular, the difficulty of measuring the fair value of the acquiree as a whole should not be underestimated (please see our response to Question 4 below). We question the reliability of this measurement and are concerned that the estimation and subjectivity involved in it will reduce the reliability of the measurement of goodwill.

The allocation of a portion of goodwill to the non-controlling interest brings further complexity. If the measurement of fair value of the acquiree as a whole is based on the consideration transferred at the acquisition date or on an income approach, the measurement of goodwill may have been affected by synergies which benefit the acquiring entity rather than the acquiree. A simple allocation on the basis of equity interest retained by the non-controlling interest would not be appropriate in this situation, but the correct allocation could be difficult to determine.

If the IASB wishes to continue with this approach, considerable further guidance on practical methods to overcome these issues must be provided.

Question 4—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?

GSK Response

We expect that in many business combinations the acquisition-date fair value of the consideration transferred in exchange for the acquirer’s interest in the acquiree may be the best evidence available of the fair value of the acquiree as a whole, but that in many cases this will not be very reliable.

We do not believe that the application guidance adequately addresses some common situations which acquiring entities will face, for example, how expectations of post-acquisition synergies which influence the amount of consideration an acquirer is willing to pay should be identified and removed when extrapolating from the fair value of the consideration paid for a portion of the acquiree to the fair value of the acquiree as a whole. The application guidance given in paragraphs A15-17 acknowledges that different entities may be prepared to pay different amounts for the same acquisition target, as well as different amounts for different proportions of the target. However, to resolve uncertainty of measurement, the main recommendation in the Application Guidance is only that the acquiring company should use market and income approaches to refine its assessment of the fair value of the target company. We note that, in Appendix E “Fair Value Measurements”, these approaches fall into level 3 in the fair value hierarchy, ie the category which has the lowest reliability of measurement. Given the prevalence of control premiums, synergies and other imperfections in the market for business entities, acquiring entities may therefore frequently have to fall back on level 3 valuation techniques in order to estimate the fair value of the acquiree as a whole. Goodwill is then measured as the residual value between this fair value and the fair value of the identifiable net assets acquired. We believe that the measurement of goodwill using a level 3 estimate as a major component of the calculation will introduce an unacceptable degree of unreliability into the measurement of goodwill.

There is also little guidance, except at a general level in Appendix E “Fair Value Measurements”, on how the fair value of an unlisted entity may be determined. More guidance on this should be provided, as most business combinations involve acquisitions of such entities.
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?

GSK Response

We agree that the fair value of the consideration transferred in exchange for an interest in the acquiree is generally the best evidence available of the fair value of that interest on that date, except where contingent consideration is concerned. In a situation where contingent consideration has been agreed between the vendor and the acquirer because of disagreement or uncertainty as to the fair value of the acquiree at that date, the subsequent remeasurement of the consideration as estimates become more certain results from the receipt of better information concerning the fair value of the acquiree at the acquisition date. This information should be used to adjust the fair value of the goodwill recognised in respect of the acquiree (or another appropriate identifiable asset or liability acquired, depending on how the amount of contingent consideration is determined), and should not result in a gain or loss in the post-acquisition income statement.

As regards the date of measurement of the consideration transferred, we agree that the date of acquisition is the most appropriate date, again with the exception of contingent consideration which should be finally measured at the date the contingent amount becomes certain.

Question 6—Is the accounting for contingent consideration after the acquisition date appropriate? If not, what alternative do you propose and why?

GSK Response

We strongly oppose this proposal which we believe will have the effect of removing contingent consideration from the options available to the negotiating parties in future business combinations. Contingent consideration enables a business combination to proceed even where there is disagreement between the vendor and the acquirer on the fair value of the acquiree. Revisions to the amount reflect a greater understanding of the fair value of the acquiree at the acquisition date and should therefore be accounted for as adjustments to the initial acquisition accounting.

A requirement to record the impact of such revisions in the income statement risks removing a useful negotiating tool, or even opening up the accounting to potential manipulation by giving acquirers an incentive to over-estimate the fair value of consideration at acquisition date in order to release gains to the income statement over subsequent periods as it becomes more certain that the contingent amount will never be paid.

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?

GSK Response

We believe that acquisition costs should be included within the measurement of consideration and hence in goodwill because they represent real value transferred in order to obtain the acquiree. Furthermore, this treatment is consistent with the treatment of acquisition costs for other assets, such as property, plant and equipment and financial assets.
Questions 8 and 9—Measuring and recognising the assets acquired and the liabilities assumed

The Exposure Draft proposes that an acquirer measure and recognise as of the acquisition date the fair value of the assets acquired and liabilities assumed as part of the business combination, with limited exceptions. (See paragraphs 28-41 and BC111-BC116.) That requirement would result in the following significant changes to accounting for business combinations:

(a) Receivables (including loans) acquired in a business combination would be measured at fair value. Therefore, the acquirer would not recognise a separate valuation allowance for uncollectible amounts as of the acquisition date.

(b) An identifiable asset or liability (contingency) would be measured and recognised at fair value at the acquisition date even if the amount of the future economic benefits embodied in the asset or required to settle the liability are contingent (or conditional) on the occurrence or non-occurrence of one or more uncertain future events. After initial recognition, such an asset would be accounted for in accordance with IAS 38 Intangible Assets or IAS 39 Financial Instruments: Recognition and Measurement, as appropriate, and such a liability would be accounted for in accordance with [draft] IAS 37 or other IFRSs as appropriate.

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?

GSK Response

We agree that the changes in respect of receivables are appropriate where a valuation adjustment can be identified for specific receivables. However, where experience suggests a proportion of the receivables will not be collected but it is not yet possible to identify which specific receivables will be uncollectible, we believe a separate valuation allowance should still be recognised as of the acquisition date.

We also agree that an identifiable asset or liability should be measured and recognised at fair value at the acquisition date even if the amount of the future economic benefits embodied in the asset or required to settle the liability are contingent (or conditional) on the occurrence or non-occurrence of one or more uncertain future events. However, consistent with paragraph 11(b) of the Exposure Draft of proposed amendments to IAS 37, we would request the Board to make clear that such liabilities should only be recognised if they are reliably measurable.

We do not agree that such liabilities should be accounted for in accordance with [draft] IAS 37 following initial recognition. As we comment in our letter on the Exposure Draft of IAS 37, we do not agree with the changes proposed in that Draft to the recognition of liabilities whose measurement is contingent upon the occurrence or non-occurrence of one or more uncertain future events. We believe that the present approach of not recognising such liabilities if an outflow of economic resources is not probable (but disclosing sufficient information about them to enable users of the financial statements to understand the risks and uncertainties involved) is appropriate. We therefore continue to believe that when such liabilities are recognised as part of the accounting for a business combination they should be measured subsequently in accordance with paragraph 48 of the current IFRS 3, i.e. they should only be remeasured in accordance with IAS 37 when an outflow of economic resources is sufficiently probable as to require recognition under that Standard (as currently written). Prior to that point, they should continue to be measured at the amount recognised in the initial accounting for the business combination.

The Exposure Draft proposes limited exceptions to the fair value measurement principle. Therefore, some assets acquired and liabilities assumed (for example, those related to deferred taxes, assets held for sale, or employee benefits) would continue to be measured and recognised in accordance with other IFRSs rather than at fair value. (See paragraphs 42-51 and BC117-BC150.)
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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?

GSK Response

We agree that these exceptions are appropriate insofar as they allow consistency of measurement between assets and liabilities acquired in a business combination and assets and liabilities generated by the entity's own operations.

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

The Exposure Draft proposes that, for the purposes of applying the acquisition method, the fair value of the consideration transferred by the acquirer would include the fair value of the acquirer's non-controlling equity investment in the acquiree at acquisition date that the acquirer owned immediately before the acquisition date. Accordingly, in a business combination achieved in stages (step acquisition) the acquirer would remeasure its non-controlling equity investment in the acquiree at fair value as of the acquisition date and recognise any gain or loss in profit or loss. If, before the business combination, the acquirer recognised changes in the value of its non-controlling equity investment directly in equity (for example, the investment was designated as available for sale), the amount that was recognised directly in equity would be reclassified and included in the calculation of any gain or loss as of the acquisition date. (See paragraphs 55, 56 and BC151-BC153.)

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?

GSK Response

We do not agree that this is the appropriate treatment of the gain or loss arising when the non-controlling interest is converted into part of a controlling interest. For other equity investments held as available-for-sale financial instruments, the movements in fair value recognised in equity since purchase are recycled to the income statement only on disposal or impairment of the investment, and we believe that the holding gain or loss on a non-controlling interest which becomes part of the consideration for a controlling interest should similarly be retained within reserves until disposal of the subsidiary concerned. As an example, if an entity acquires 4 per cent of another entity in one transaction and then at a later date pays a higher per share value for the remaining 96 per cent, it seems illogical that this should give rise to a gain in the income statement on revaluation of the 4 per cent holding, which is still owned by the entity.

The Exposure Draft proposes that in a business combination in which the consideration transferred for the acquirer's interest in the acquiree is less than the fair value of that interest (referred to as a bargain purchase) any excess of the fair value of the acquirer's interest in the acquiree over the fair value of the consideration transferred for that interest would reduce goodwill until the goodwill related to that business combination is reduced to zero, and any remaining excess would be recognised in profit or loss on the acquisition date. (See paragraphs 59-61 and paragraphs BC164-BC177.) However, the proposed IFRS would not permit the acquirer to recognise a loss at the acquisition date if the acquirer is able to determine that a portion of the consideration transferred represents an overpayment for the acquiree. The boards acknowledge that an acquirer might overpay to acquire a business, but they concluded that it is not possible to measure such an overpayment reliably at the acquisition date. (See paragraph BC178.)

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?
GSK Response

We do not agree that, where the fair value of the interest obtained is greater than the consideration transferred, and all goodwill on that business combination has been reduced to zero, the remaining excess should be recognised in profit or loss on acquisition date. As noted in our response to Question 5 above, we support the contention that the amount paid for an investment is the best evidence of its fair value. To recognise a profit in this situation completely contradicts this presumption. Furthermore, we believe that to allow a profit to be created through a fair value measurement exercise on acquisition is unwise as it sets subjective judgements over the evidence provided by an open market arm’s length transaction and could be open to manipulation. Although we recognise that the concept of recognising a credit in the income statement in such a situation already exists in IFRS 3, we believe that such an excess should be recorded within equity and recognised in the income statement only in the event of the subsidiary being disposed of at a later date.

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?

GSK Response

We note that overpayments above the fair value of an entity as a standalone entity may frequently occur for rational reasons, for example where an acquirer is prepared to pay more to secure control of an entity due to strategic benefits or expected synergies which do not apply to other potential acquirers in the marketplace. We believe that such “overpayments” purchase genuine value for the acquirer and it is therefore appropriate that they should remain as assets in the acquirer’s balance sheet.

We also support the view that it is more appropriate to recognise real overpayments, perhaps arising because of a lack of understanding of the fair values of the acquiree which is not rectified until after the business combination, as an immediate loss. However, we agree that, because of the difficulty in reliably measuring the fair value of an acquiree, it will be difficult to identify such overpayments and that the treatment proposed is therefore a pragmatic approach to this problem. We believe this to be an acceptable approach, particularly as subsequent impairment tests of the goodwill arising in a business combination will provide an alternative route, after the initial accounting for the business combination, for recognising such losses in the income statement in the form of impairments.

We also note that the boards’ conclusion that it is not possible to measure an overpayment appears to acknowledge the difficulty inherent in measuring the fair value of an acquiree (discussed in our response to Question 5 above), which is one of our principle concerns with the proposal to apply the full goodwill method. If it is possible to measure with reliability the fair value of an acquiree, why is it not possible to measure the overpayment above fair value?

Question 13—Measurement period

The Exposure Draft proposes that an acquirer should recognise adjustments made during the measurement period to the provisional values of the assets acquired and liabilities assumed as if the accounting for the business combination had been completed at the acquisition date. Thus, comparative information for prior periods presented in financial statements would be adjusted, including any change in depreciation, amortisation or other profit or loss effect recognised as a result of completing the initial accounting. (See paragraphs 62-68 and BCl61-BC163.)

Question 13—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?
GSK Response

We do not agree that comparative information should be restated for the effects of measurement period adjustments. These should be accounted for prospectively as they generally represent changes in accounting estimates, rather than errors. We also believe that adjusting comparative information will reduce the understandability of the financial statements for users who generally prefer to focus on the current period and not to have to revisit comparative periods for potentially quite small changes. It is conceivable that the proposal to require comparative information to be adjusted could provide a disincentive to some entities to make such adjustments and hence lead to a lowering of the quality of information within the financial statements.

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

The Exposure Draft proposes that an acquirer assess whether any portion of the transaction price (payments or other arrangements) and any assets acquired or liabilities assumed or incurred are not part of the exchange for the acquiree. Only the consideration transferred by the acquirer and the assets acquired or liabilities assumed or incurred that are part of the exchange for the acquiree would be included in the business combination accounting. (See paragraphs 69, 70, A87-A109 and BC154-BC160.)

Question 14—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?

GSK Response

We agree that it is appropriate to separately identify and account for any portions of the transaction price and assets acquired or liabilities assumed which are not part of the exchange for the acquiree, and that sufficient guidance is provided.

Question 15—Disclosures

The Exposure Draft proposes broad disclosure objectives that are intended to ensure that users of financial statements are provided with adequate information to enable them to evaluate the nature and financial effects of business combinations. Those objectives are supplemented by specific minimum disclosure requirements. In most instances, the objectives would be met by the minimum disclosure requirements that follow each of the broad objectives. However, in some circumstances, an acquirer might be required to disclose additional information necessary to meet the disclosure objectives. (See paragraphs 71-81 and BC200-BC203.)

Question 15—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?

GSK Response

We agree that the disclosure objectives and minimum disclosure requirements appear reasonable.

Questions 16-18—The IASB’s and the FASB’s convergence decisions

The Exposure Draft is the result of the boards’ projects to improve the accounting for business combinations. The first phase of those projects led to the issue of IFRS 3 and FASB Statement No. 141. In 2002, the FASB and the IASB agreed to reconsider jointly their guidance for applying the purchase method of accounting, which the Exposure Draft calls the acquisition method, for business combinations. An objective of the joint effort is to develop a common and comprehensive standard for the accounting for business combinations that could be used for both domestic and cross-border
Although the boards reached the same conclusions on the fundamental issues addressed in the Exposure Draft, they reached different conclusions on a few limited matters. Therefore, the IASB's version and the FASB's version of the Exposure Draft provide different guidance on those limited matters. A comparison, by paragraph, of the different guidance provided by each board accompanies the draft IFRS. Most of the differences arise because each board decided to provide business combinations guidance that is consistent with its other standards. Even though those differences are candidates for future convergence projects, the boards do not plan to eliminate those differences before final standards on business combinations are issued.

The joint Exposure Draft proposes to resolve a difference between IFRS 3 and SFAS 141 relating to the criteria for recognising an intangible asset separately from goodwill. Both boards concluded that an intangible asset must be identifiable (arising from contractual-legal rights or separable) to be recognised separately from goodwill. In its deliberations that led to SFAS 141, the FASB concluded that, when acquired in a business combination, all intangible assets (except for an assembled workforce) that are identifiable can be measured with sufficient reliability to warrant recognition separately from goodwill. In addition to the identifiability criterion, IFRS 3 and IAS 38 required that an intangible asset acquired in a business combination be reliably measurable to be recognised separately from goodwill. Paragraphs 35-41 of IAS 38 provide guidance for determining whether an intangible asset acquired in a business combination is reliably measurable. IAS 38 presumes that the fair value of an intangible asset with a finite useful life can be measured reliably. Therefore, a difference between IFRS 3 and SFAS 141 would arise only if the intangible asset has an indefinite life.

The IASB decided to converge with the FASB in the Exposure Draft by:

(a) eliminating the requirement that an intangible asset be reliably measurable to be recognised separately from goodwill; and

(b) precluding the recognition of an assembled workforce acquired in a business combination as an intangible asset separately from goodwill. (See paragraphs 40 and BC100-BC102.)

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? Do you have any examples of an intangible asset that arises from legal or contractual rights and has both of the following characteristics:

(a) the intangible asset cannot be sold, transferred, licensed, rented, or exchanged individually or in combination with a related contract, asset, or liability; and

(b) cash flows that the intangible asset generates are inextricably linked with the cash flows that the business generates as a whole?

GSK Response

We do support the principle, already in current IFRS 3, that intangible assets should be recognised separately from goodwill, wherever possible. However, we do not agree that it is always possible to reliably measure any intangible asset acquired in a business combination. The fact that it has been acquired in a business combination does not necessarily mean it is reliably measurable. While the total consideration transferred for the interest acquired has the credibility of having been agreed in an arm's length transaction with another party, the allocation of this total amongst the various assets and liabilities acquired, including goodwill, requires estimation and judgement if external market prices for similar assets are not available. This estimation and judgement reduces the reliability of the measurement.

As an example of intangible assets that cannot be reliably measured, we would point out the difficulty of determining fair values for individual early-stage R&D projects within a pipeline of in-process R&D (IPR&D) projects. The failure rate of early-stage projects in an industry such as pharmaceuticals is such that any individual project is more likely to fail than not. Although it is possible to estimate the fair value of the IPR&D as a whole, it is not possible to determine which individual projects within it will have value and which will have none. Attempting to assign a probably-adjusted individual fair value to each project inevitably means that the total carrying value of the projects is reduced over subsequent
periods as projects fail and impairment write-downs are recorded, yet in reality the fair value of the IPR&D as a whole is not impaired provided the expected proportion of projects does succeed. In more general terms, we do not believe that fair values can reliably be assigned to specific items in a group of similar assets that do not yet generate cash flows but where some items from the group will generate cash flows in the future but some will not.

For the joint Exposure Draft, the boards considered the provisions of IAS 12 Income Taxes and FASB Statement No. 109 Accounting for Income Taxes, relating to an acquirer’s deferred tax benefits that become recognisable because of a business combination. IAS 12 requires the acquirer to recognise separately from the business combination accounting any changes in its deferred tax assets that become recognisable because of the business combination. Such changes are recognised in post-combination profit or loss, or equity. On the other hand, SFAS 109 requires any recognition of an acquirer’s deferred tax benefits (through the reduction of the acquirer’s valuation allowance) that results from a business combination to be accounted for as part of the business combination, generally as a reduction of goodwill. The FASB decided to amend SFAS 109 to require the recognition of any changes in the acquirer’s deferred tax benefits (through the reduction of the acquirer’s previously recognised valuation allowance) as a transaction separately from the business combination. As amended, SFAS 109 would require such changes in deferred tax benefits to be recognised either in income from continuing operations in the period of the combination or directly to contributed capital, depending on the circumstances. Both boards decided to require disclosure of the amount of such acquisition-date changes in the acquirer’s deferred tax benefits in the notes to the financial statements. (See paragraphs D4 and BC119-BC129.)

Question 17—Do you agree that any changes in an acquirer’s deferred tax benefits that become recognisable because of the business combination are not part of the fair value of the acquiree and should be accounted for separately from the business combination? If not, why?

GSK Response

We agree with this decision.

The boards reconsidered disclosure requirements in IFRS 3 and SFAS 141 for the purposes of convergence. For some of the disclosures, the boards decided to converge. However, divergence continues to exist for some disclosures as described in the accompanying note Differences between the Exposure Drafts published by the IASB and the FASB. The boards concluded that some of this divergence stems from differences that are broader than the Business Combinations project.

Question 18—Do you believe it is appropriate for the IASB and the FASB to retain those disclosure differences? If not, which of the differences should be eliminated, if any, and how should this be achieved?

GSK Response

We support the objective of convergence and regret that such differences remain. However, we accept that this may be a practical necessity in order to allow the proposals in this stage of the business combinations project to be publicly aired and discussed.

We trust that the differences that remain will not be a hindrance in the achievement of acceptability of IFRS financial statements in the US without the need for reconciliation to US GAAP, which was identified as an objective for 2009 in the “Road Map” laid out by the SEC in April 2005.

Question 19—Style of the Exposure Draft

The Exposure Draft was prepared in a style similar to the style used by the IASB in its standards in which paragraphs in bold type state the main principles. All paragraphs have equal authority.
Question 19—Do you find the bold type-plain type style of the Exposure Draft helpful? If not, why? Are there any paragraphs you believe should be in bold type, but are in plain type, or vice versa?

GSK Response

We do find this style helpful and have not identified any paragraphs which appear to be in the wrong type.
• We do not agree with the proposed changes in respect of subsequent remeasurement of contingent liabilities acquired in a business combination. We believe that the current treatment, whereby acquired contingent liabilities are not remeasured unless the liability qualifies for recognition under (current) IAS 37, is more appropriate. As we state in our letter of today's date commenting on the Exposure Draft of IAS 37, we do not agree that obligations with a remote possibility of outflow of economic resources or whose measurement is contingent upon the occurrence or non-occurrence of uncertain future events should be recognised in the balance sheet, except in the case where they influence the consideration paid for an acquiree in a business combination. We therefore do not agree that changes in measurement of acquired liabilities should affect profit or loss until the liability is sufficiently probable to warrant recognition in its own right under (current) IAS 37.

• In our view, acquisition costs represent real value transferred in order to obtain the acquiree, and it is appropriate that they should be included in the acquisition accounting. We find no merit in the view that they should be treated differently from acquisition costs on the purchase of any other asset.

The appendices attached to this letter provide responses to the questions set out by the IASB in its invitations to comment on each of the Exposure Drafts. In our responses we have highlighted the key points we wish to make by the use of bold text.

Please contact me if you would like to discuss further any points in this letter.

Yours sincerely,

Mr PF Blackburn
Financial Controller
GlaxoSmithKline plc