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Le Président

AB/PS/MCG

N°

Paris, 26th October 2005

Sir David Tweedie
Chairman I.A.S.B.
30 Cannon Street
London EC4M6XH

Re: IASB's Exposure draft of Proposed Amendment to IFRS 3 *Business Combinations*, IAS 27 *Consolidated and Separate Financial Statements*, IAS 37 *Provisions, Contingent Liabilities and Contingents Assets* and IAS 19 *Employee Benefits*

Dear Sir David,

I am writing on behalf of the CNC to comment on the above mentioned Exposure Drafts.

As we have major reservations about important aspects of the timing of the exposure drafts and about their content, we summarise these reservations in this letter. Our answers to the detailed questions raised in the Exposure Drafts are presented in Appendix 1.

We are highly concerned with the pace of changes introduced by the IASB just after the first adoption of the "stable platform" of standards by listed companies in Europe. We are therefore concerned with the timing of the Exposure Drafts which modify only recently implemented standards and do so without an in-depth discussion of conceptual changes which depart from the Framework and which will be impacted in the near future by other major projects of the IASB (or the IASB and the FASB) such as the Measurement project, the proposed implementation guidance on applying fair value, the performance reporting project and the consolidation project with a potential new definition of control.

We disagree with important aspects of the Exposure Drafts, mainly:

- the measurement of an acquired business at its fair value rather than its cost;
- the economic entity approach to consolidated financial statements versus the approach currently used in IFRS 3; and
- the withdrawal of probability as a recognition criterion in IAS 37

The measurement of an acquired business at its fair value rather than its cost:

We disagree with the proposal in the Exposure Draft that an acquired business should be measured as a whole at its fair value rather than at its cost for the following reasons, which are further developed in our detailed answers to the questions, raised by the Board:

- We do not believe that in Basis for conclusion paragraph BC 18 (b) the Board has demonstrated that the proposed change will improve the quality of information provided in consolidated financial statements as we have serious doubts on the existence of the fair value of an acquiree as defined in the Exposure Draft. Each potential acquirer has its own objectives resulting from its existing position on the market and from its strategy and we doubt that, because of that, two potential acquirers would ever come up with the same fair value for a specific acquiree.
- We agree with the dissenting Board Members that the total fair value of an acquired business is an extremely subjective measure which will be difficult to derive from the consideration transferred as the acquirer does not necessarily determine its pricing solely on the basis of the acquiree's fair value but also on the synergies which it may be the only potential acquirer to expect. We also see major practical difficulties in measuring the total fair value of the acquiree when the transaction is for materially less than 100% which is often the case in business combinations in Europe. We also believe that such practical difficulties will result from the present lack of fair value measurement guidance in IFRS's.
- The approach proposed in the Exposure Draft introduces two different measurement principles for the acquisition of assets or groups of assets (cost) and for the acquisition of businesses or groups of businesses (fair value) when the proposed guidance broadens the definition of a business to a point where the difference between a group of assets and a business becomes very thin.
- The Exposure Draft introduces major limitations to the fair value principle in cases of overpayments or underpayments thus reducing the expected benefits of the proposed change when imposing material additional costs;

We therefore believe that the proposed approach will generate material additional costs for financial information which is not more relevant and useful but less reliable that under existing standards. We therefore recommend keeping the cost measurement of business combinations as in the existing IFRS 3.

Economic Entity Approach of Consolidated Financial Statements versus the approach currently in IFRS 3

We disagree with the proposal in the Exposure Drafts that the "economic entity approach" should be used for the preparation of consolidated financial statements rather than the current "mixed" approach under IFRS 3. Such a choice drives many fundamental changes including recognising the non-controlling interests' share of goodwill, the accounting for decreases and increases in ownership interests of a parent company after control is obtained and the allocation of losses between the parent company and the non-controlling interests.

We believe that the "parent company approach» has more merits for the information of users than the "economic entity approach" which inevitably widens and dilutes the relevance of the consolidated financial statements for the investors in the parent entity. Indeed we do not believe that the Board has demonstrated that the "economic entity approach" provides more relevant and useful information; on the contrary we believe that the choice in the Exposure Draft of an "economic entity" only approach will deprive the parent company shareholders of valuable information especially in Europe and particularly in France where large non-controlling interests are frequently encountered in practice. Paragraphs 9 & 10 of the conceptual Framework note that, although there are many potential users of financial statements, investors are considered to be the primary users. We do not believe that information related to full goodwill would be relevant to the investors providing risk capital to the parent company. We are also not fully convinced that the Board has taken into consideration the various laws governing the rights of non-controlling shareholders in its proposal.

While we agree with the Board that non-controlling interests do not meet the definition of a liability and therefore should be presented in equity as required by IAS 27, we support the views expressed by dissenting Board Members that such interests represent claims that are restricted to particular subsidiaries, whereas the controlling interests are affected by the performance of the entire group. Although the non-controlling interests are presented in equity, we believe they are a different kind of equity and consequently we do not therefore believe that, the mere fact that they are presented in equity leads to the rejection of the existing mixed approach under IFRS 3.

One of the consequences of adopting the "economic entity" approach is the recognition of the non controlling interests' share of goodwill. We have strong reservations about this change as we believe that the proposed accounting treatment gives irrelevant and useless information on the subsequent acquisition of non-controlling interests by the parent when the subsidiary has been largely developed after the acquisition of the control. Applying the proposed accounting would lead to a material decrease in parent's and in the consolidated equity at the date an additional interest is acquired at fair value in a successful business.

As explained above, we believe that the proposed "economic entity" only approach will deprive the shareholders of the parent entity of relevant and useful information especially in countries where large non-controlling interests are a common practice, and will create new difficulties which do not exist under the existing standards. We therefore recommend keeping the current "mixed approach" under IFRS 3 for consolidated financial statements.

Withdrawal of probability as a recognition criterion in IAS 37

We disagree with the proposal in the Exposure Drafts that probability be withdrawn as a recognition criterion for non-financial liabilities in IAS 37 for the following main reasons which are further developed in our answers to the detailed questions raised by the Board:

- We disagree with the proposal, which we believe is in breach of the recognition criteria for a liability in the conceptual framework. We also note that the proposed definition of a liability still includes an "expected outflow of resources" and that therefore the new recognition criterion contradicts the proposed definition of a liability.
- We also believe that measuring "single events" liabilities at exit value requires a high degree of subjectivity and is **not relevant to predict future cash flows in the ordinary course of business**. We therefore question the relevance of such proposal.
- We do not believe that in the Exposure Draft the triggering event of an unconditional obligation (stand ready obligation) is clearly defined and this lack of precision constitutes a major weakness as the same situation may lead to different accounting (recognising or not recognising a non financial liability).

- We believe that the Board failed to demonstrate that the benefits to be obtained from the change are superior to the costs derived. We also consider that such proposal is anticipating conclusions that might be reached in the Insurance Contracts Accounting project.

Process followed by the Board

The changes proposed in the Exposure Drafts represent major changes whereas First Time Adopters only start to experience the IASB Stable Platform. For this reason we regret that the Board did not first issue a Discussion paper to present the major conceptual changes introduced by the proposals. We also regret that the Board did not conduct field tests in Europe and particularly in France in view of the greater challenges that most preparers and auditors will face implementing the proposals, particularly in relation to the presence of large non-controlling interests in most European countries.

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In conclusion, we recommend that the Board postpones the issuance of revised standards in order to leave time to European and other First Time Adopters to gain experience in applying current IFRS 3; this should help better identify the problems mostly encountered in practice and determine whether changes to this standard are actually needed. If major amendments are then considered, we believe that additional field-testing with both preparers and users should be conducted, especially in Europe. We also believe that before amending the existing standards the Board should advance or complete other projects which are closely related (fair value, measurement, consolidation, performance reporting…).

In the immediate future, any amendments to the existing standards should be restricted to accounting requirements for increase and decrease of interest after control is obtained, based on the existing IFRS 3 approach to consolidated financial statements, However, we also recommend that the Board starts considering additional guidance which is critically lacking in the field of accounting for the creation of joint ventures and business combinations of entities under common control.

We would be pleased to discuss our comments or give you further clarification. In this connection please contact me or Philip Staines at the CNC or Dominique Thouvenin.

Kind regards,

Antoine BRACCHI

ED OF PROPOSED AMENDMENTS 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.*

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)*
- *(d) in which the acquirer holds less than 100 per cent of the equity interests in the acquiree 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?

CNC Comments

We do not agree with the objective described under paragraph 1 of the Exposure Draft for the reasons developed below:

- **Even if we are not opposed in principle to a change of the definition of a business combination, we, however, strongly disagree with paragraph BC 32 of the basis for conclusions that states that all business combinations included in the scope of IFRS 3 are covered by the new definition proposed in the Exposure Draft. We consider that, as opposed to existing provisions of IFRS 3, the definition in the Exposure Draft excludes from its scope true mergers and business combinations where there is no acquirer including most business combinations involving mutual entities and dual listed entities. Therefore, we disagree with the fact that a comment in a Basis for conclusions could amend the definition by explaining that the proposed IFRS will not change the current scope.**

- **As we had already indicated in our comment letter on ED 3, we still believe that the identification of an acquirer may be impossible in certain circumstances and that the application of the acquisition method in that case would clearly be inappropriate and would lead to an accounting treatment that does not reflect the economic reality. For those reasons, we strongly encourage the Board to complete its work on the fresh start method and the comparison with the pooling method to ascertain whether the fresh start method is a better method.**

- **We also disagree with the statement in the objective that the acquirer measures the acquiree as a whole at its fair value:**

  ✓ **As the Board, we believe that acquisitions of assets and acquisitions of businesses should be accounted in the same way and we therefore disagree with the proposed introduction of two different accounting methods (see our answer to question 2).**

  ✓ **We also note the difficulties encountered by the Board on the application of the fair value measurement of the acquiree and the important restrictions to the principle in cases of overpayments and underpayments (see our answer to questions 11 and 12).**

  ✓ **We agree with the dissenting Board Members that the total fair value of an acquired business is an extremely subjective measure which, in many cases, will be difficult to derive from the consideration transferred as the acquirer does not necessarily determine its pricing solely on the basis of the acquiree's fair value but also on criteria which are specific to him such as the synergies which it may be the only potential acquirer to expect, its existing market share and its intention to achieve market leadership, its intention to eliminate a competition or its decision to enter a new market. Its value is by definition a subjective value and we therefore do not believe that the concept of a single fair value for an acquiree is relevant. The range of possible valuations for the fair value of the entire acquiree is likely to introduce much greater subjectively than the cost approach.**

- ✓ **We also see major practical difficulties in measuring the total fair value of the acquiree when the actual transaction is for materially less than 100% of the acquiree which is often the case in business combinations in France (See our answer to question 3).**
- ✓ **We agree with the comments made by the Board members during their September 2005 meeting on the "confusion that exists among constituents as a result of the lack of consistent, integrated guidance in IFRS's on fair value measurements" and we recommend that discussions and approval of the future exposure draft on fair value measurement be finalized before the Exposure Draft on IFRS 3 is turned into a final standard.**

We believe that the introduction of the measurement at fair value of the entire acquiree is likely to lead to material extra costs whilst providing more subjective and less reliable information to users of financial statements. We therefore propose to keep the cost measurement of business acquisitions as in the existing IFRS 3.

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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?

CNC comments

We agree with the Board when it concludes under paragraph BC 41 that acquisitions of assets and businesses should be accounted for in the same way. We are therefore concerned that acquisitions of assets would still be accounted for at cost whereas in the Exposure Draft acquisitions of businesses would be accounted for at fair value. In our view acquisitions of businesses should remain accounted for at cost as it is the case under the present IFRS 3.

We are convinced that if they are not, the difference between both accounting treatments should have substance. We do not believe this is the case with the proposed definition of a business and with the additional guidance in the Exposure Draft. Actually, the introduction of the notion of "capable of being conducted or managed" would largely broaden the scope of situations that could satisfy the definition of a business. The distinction would be too narrow as in our view, most assets or groups of assets are capable of being conducted or managed as a business (e.g. a non-producing oil field could be interpreted to be a business). We are highly concerned that the narrow dividing line between the definition of a business and certain assets or groups of assets would lead, if the Exposure Drafts were adopted, to major difficulties and inconsistencies in applying the definition. The risk would be significant for transactions of similar economic substance to receive different accounting treatment.

We believe that the Board should reconsider the introduction of the term "capable of" in the proposed definition which we believe is too broad.

We also recommend that the Standard's implementation guidance contain several examples of groups of activities and assets that are and are not businesses in order to assist in the interpretations of the Standard.

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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?

CNC comments

Although we understand the conceptual approach of the Board in requiring the recognition of 100 per cent of the value of goodwill at acquisition date, we disagree with the Board that the proposed approach will produce more relevant and more useful information for the users of consolidated financial statements:

The proposed accounting treatment gives irrelevant and useless information on the subsequent acquisition of non-controlling interests of a subsidiary by the parent when the subsidiary has been largely developed since the control acquisition. Applying such accounting would lead to a material decrease in parent's equity at the date an additional interest in a successful business is acquired while, at the same time, that transaction gives the parent company the right to access to future economic benefits that were previously attributed to minority interests.

We also agree with the dissenting Board members (AV5) that not only the total value of the acquired business is difficult to measure but so is the allocation of the goodwill between the parent and the non-controlling interests:

- **There is a difficult process of stripping out the synergies attributable only to the parent company.**
- **It would involve measuring the control premium which is not discussed in the Exposure Draft.**

Alternative to the proposed approach

In our view, the price paid for an acquisition is a more objective and reliable measurement basis for the acquiree. Moreover the goodwill derived from that value, which is a reflection of the parent company's strategy, is more relevant than the total goodwill of the economic entity. We therefore recommend maintaining the "cost" basis for valuing the acquiree and the parent company approach to goodwill valuation. These views are consistent with those expressed by dissenting Board members in AV 2 to AV7.

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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.)*

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?

CNC Comments

We believe that application guidance in the Exposure Draft is insufficient as:

- **No example takes into account the potential existence of a control premium which would justify that the price of the controlling interest maybe higher than the price for the non controlling interest.**
- **It does not address examples for non listed companies. We also note an inconsistency between the Exposure Draft which always requires to determine the fair value of non listed shares and IAS 39 which allows measurement of available for sale of investments in non listed equity instruments at cost when fair value cannot be reliably determined (IAS 39.46 (c)).**
- **There is no example for contingent consideration which is used mainly in cases where acquirer and seller disagree on the fair value such as the acquisition of a start up company.**
- **The only example which could be the most useful to allocate goodwill between parent and non controlling interest (example 3) is flawed as it only deals with synergies only available to the acquirer and not with a potential control premium.**

Furthermore, we strongly regret that appendix E is subject to the finalization of FASB project on measurement and we recommend that it is reexposed if amended.

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The Exposure Draft proposes a presumption that the best evidence of the fair value of the acquirer's interest in the acquiree would be the fair values of all items of consideration transferred by the acquirer in exchange for that interest measured as of the acquisition date, including:
(c) contingent consideration;
(b) equity interests issued by the acquirer; and
© any non-controlling equity investment in the acquiree that the acquirer owned immediately before the acquisition date. (See paragraphs 20-25 and BC55-BC58.)

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?

CNC Comments

We agree as in IFRS 3 that the <u>acquisition-date fair value</u> of the consideration is the best evidence of the <u>cost</u> of the interest acquired but we believe that the fair value of the consideration <u>at the agreement date</u> is a better indicator of <u>the fair value</u> of the interest acquired.
In certain circumstances the acquiree may be measured at the date of acquisition at an amount that is not the acquiree's fair value at that date. This might be the case when, for example, the combination is effected through a transfer of the acquirer's equity instruments the market value of which (eg published price of the quoted share transferred) having decreased for reasons unrelated to the business combination between the agreement date (date at which the parties agreed to combine and at which the fair value of the acquiree has been measured) and the acquisition date. In that case, the decrease in the market value of the acquirer's shares may lead to the recognition of the acquiree at an amount that might obviously differ from the fair value of the acquiree. Under the cost approach this difficulty is avoided.

Although we agree that, as it is partially the case in current IFRS 3 [1], any non controlling interest previously held by the acquirer should be revalued to its fair value at the date control is obtained, we strongly disagree that the fair value of the consideration transferred used to determine the fair value of the acquiree should include the fair value of any non controlling interest previously held by the acquirer as such interest is not part of the exchange transaction.

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The Exposure Draft proposes that after initial recognition, contingent consideration classified as:
(a) equity would not be remeasured.
(b) liabilities would be remeasured with changes in fair value recognised in profit or loss unless those liabilities are in the scope of IAS 39 Financial Instruments: Recognition and Measurement or [draft] IAS 37 Non-financial Liabilities. Those liabilities would be accounted for after the acquisition date in accordance with those IFRSs.
(See paragraphs 26 and BC64-BC89.)

[1] Under current IFRS 3, any revaluation at fair value of the net asset acquired in a Business Combination achieved in stages, relating to the previously held interests shall be accounted for as a revaluation surplus.

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

CNC Comments

As already indicated, we believe contingent consideration is mainly used in business combinations where acquirer and seller cannot agree on the fair value of the acquiree. We therefore consider that the fair value of contingent consideration will be very difficult to determine reliably at the acquisition date. This will be the case where, for example, the contingency relates to the value of the business acquired or where the acquiree is a start up or an early stage business. Requiring a value to be determined at acquisition date may result in unreliable and inappropriate measurement of the acquiree.

We consider current treatment under the cost approach in IFRS 3 more appropriate due to the lack of reliability of the initial measurement of the contingent consideration in most cases.

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The Exposure Draft proposes that the costs that the acquirer incurs in connection with a business combination (also called acquisition-related costs) should be excluded from the measurement of the consideration transferred for the acquiree because those costs are not part of the fair value of the acquiree and are not assets. Such costs include finder's fees; advisory, legal, accounting, valuation and other professional or consulting fees; the cost of issuing debt and equity instruments; and general administrative costs, including the costs of maintaining an internal acquisitions department. The acquirer would account for those costs separately from the business combination accounting. (See paragraphs 27 and BC84-BC89.)

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?

CNC Comments

We believe that the Exposure Draft is inconsistent with other IFRSs including IAS 39 which requires most financial instruments to be initially measured at fair value plus any directly attributable transaction costs. That measurement is required for all financial assets and liabilities even for instruments such as Available for sale financial assets that are subsequently re-measured at fair value through equity.

We therefore prefer the existing cost approach in IFRS 3 which is consistent with other standards for the accounting for transaction costs.

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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?

CNC comments

We agree that receivables (including loans) should be measured at fair value with no separate valuation allowance.

We note that the probability criterion for recognising assets and liabilities has been abandoned as stated in BC 97 because the Board considers that « in all cases an unconditional right or obligation satisfies the criterion ». It is proposed to use the probability criterion in the measurement of these rights and obligations. We strongly disagree with that conceptual change and we consider that probability should be kept as a recognition criterion.

Furthermore, we do not believe that the triggering event of an unconditional obligation (or right) is clearly defined (see our comments on IAS 37). We consider that the proposed guidance does provide any clear assistance in determining when an obligation becomes unavoidable for exemple in a lawsuit. Is it sufficient for a party to recognise its responsibility or must legal proceedings be engaged?

We disagree that the reliability of measurement is not kept as a recognition criterion in the draft standard on the basis it is part of the framework. We believe this criterion should be maintained as we understand that a standard has overriding authority as compared to the Framework. In addition, we totally agree with the comments made by the dissenting Board member (paragraph AV 19) that this omission may lead to recognizing assets and liabilities whose value is based on unreliable measurement which creates major inconsistencies with one of the qualitative characteristics of the financial statements (paragraph 31 of the framework).
We also strongly disagree that all acquired intangible assets can be reliably measured (see answer to question 16).

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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.)

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?

CNC comments

We agree with the proposed exceptions. However, we refer to our comments made on the previous question as regards to the proposed amendment concerning the reliability measurement criterion.

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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?

CNC comments

We do not agree with the Board's comments that the change in the fair value of the acquirer's non controlling equity investment in the acquiree be recognised through profit or loss at the date of acquisition as if it had been disposed of and immediately repurchased. As we support the cost approach in IFRS 3 for business combinations we do not accept revaluation of previously acquired goodwill. Such reevaluation would also contradict IAS 38 which forbids the reevaluation of internally developed goodwill.
We consider that the decision as to whether the change in the fair value of the non-controlling interest (i.e. change corresponding to the revaluation gain on identifiable assets and liabilities) should be accounted for in profit or loss, should be delayed to the completion of the performance reporting project.

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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?

CNC comments

We strongly believe that the comments made by the Board in BC 164 to BC 177 are a clear illustration of the problems related to the measurement of acquisition at fair value. We particularly note that in paragraph BC 175 the proposal made by the Board to reduce goodwill for the excess of the fair value of the interest over the consideration transferred contradicts statement made previously (BC 37) that goodwill meets the definition of an asset. These comments highlight the fact that the fair value approach in recognizing an acquiree is rather premature and that the conceptual debate as to whether such approach should be adopted when accounting for a business combination, must be postponed until advanced principles have been developed on measurement issues.
We concur with the Board that this limitation on gain recognition is inconsistent with the general principle underlying the Exposure Draft (that the acquirer should recognise the fair value of the business acquired) and could lead to certain transactions being misrepresented.

We do not understand why such practical exceptions to the general principle have not been introduced in other areas of the ED where similar issues arise.

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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?

CNC comments

If the Board believes that the fair value of an acquiree and the fair value of the consideration transferred can be measured reliably, we do not see any problem to reliably measure an overpayment.

We disagree with the Board that an overpayment (when the acquirer pays an amount that is more than the fair value of its interest in the acquiree) is only theoretical probability. For the reasons already indicated we believe that the amount paid by the acquirer depends on the particular situation and motivation of that acquirer e.g existing market share and acquisition of leadership, entrance ticket to a market, elimination of a competitor or specific synergies available only to the acquirer and will frequently be different from value of the acquiree for the other potential acquirers (the market).

As already indicated, we also believe that the fact that the fair value of the consideration transferred is measured at acquisition date and not at agreement date may often be an identified cause for an overpayment.

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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 BC161-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?

CNC comments

We consider the adjustment period as a practical improvement from the existing IFRS 3; However, as a practical approach, we propose to extend the rebuttable presumption included in the amendments to IAS 12 to all valuation adjustments made during the measurement period.

We also agree that the restatement of comparative figures for prior periods to take into account the effects of measurement period adjustments provides more relevant information to users of consolidated financial statements.

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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?

CNC comments

We agree that the guidance provided is sufficient for making the assessment of whether any portion of the transaction price is not part of the exchange, however, we do not believe that such guidance is clear in relation to assets acquired or liabilities assumed as we cannot identify transactions made for the benefit of the acquiree that do not benefit to the combined entity. In other words, we do not see how it is possible to identify a transaction (assets acquired or liabilities assumed) that is arranged primarily for the economic benefit of the acquiree and which has no impact for the combined entity. Since the acquiree is part of the combined entity as of the date of acquisition, the transaction will automatically have an economic impact on the combined entity.

We also consider that the example for identifying assets acquired or liabilities assumed which should be excluded from the exchange transaction is unclear.

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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?

CNC comments

We agree with the disclosures objectives and the minimum disclosures requirements ; however in view of the stated convergence objective we believe that the disclosure requirements of the IASB and FASB Exposure Draft's should be aligned :

- **§76 (d) Disclosure of the financial effects of the amounts recognised in a business combination is not part of the FASB guidance and should be removed**
- **§ 78 (b) of the FASB ED which requires disclosure of goodwill by reportable segment should also be added to the IASB ED.**

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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 financial reporting. 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?

CNC comments

We do not believe that an identifiable intangible asset can always be measured reliably as we have identified intangible assets arising from legal or contractual rights which cannot be sold or transferred separately such as:

- **Business operating licenses that cannot, as part of the conditions, be sold as they are attached to the entity which was granted the license (casinos,…)**
- **Other specialized rights that are also restricted from sale such as water acquisition rights.**
- **Brands which are the name of the entity**

We do not accept such a proposed amendment when the only reason stated in the basis for conclusion is to converge with the FASB pronouncements even though it is clearly admitted that it will imply a significant degree of judgment in determining the fair value. In our opinion, the considerable emphasis placed by existing accounting standards worldwide on the need for reliable measurement of intangible assets much more than other assets, is a clear indication that the fair value estimates for some intangible assets are far more subjective and arbitrary than the fair value measurements of other assets.
We therefore believe that reliable measurement should be maintained as one of the criteria to recognize an intangible asset separately from goodwill

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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 a change in 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?

CNC comments

We agree that any changes in an acquirer's deferred tax benefits that become recognizable because of the business combination should be accounted for separately from the business combination.

As a consequence, we believe that paragraph 80 of the Exposure Draft should have been modified to drop subparagraph (c) which becomes irrelevant.

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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?

CNC comments

In view of the objective of convergence, it is regrettable that some divergence between IASB and FASB remains due to differences stemming from standards outside the business combination projects, as this is likely to lead to further future amendments to IFRSs and reduce the comparability of financial information from one period to another.

We have identified, in our answer to question 15, some disclosure items where we consider the IASB could advantageously adopt the same requirements as FASB and therefore diminish these divergences:

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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?

CNC comments

We principally agree with the bold type – plain type distinction and find it helpful. We have not (yet) identified any paragraphs which should be changed from one typeface to another.

ED OF PROPOSED AMENDMENTS TO IAS 27 *Consolidated and Separate Financial Statements*

Question 1

Draft paragraph 30A proposes that changes in the parent's ownership interest in a subsidiary after control is obtained that do not result in a loss of control should be accounted for as transactions with equity holders in their capacity as equity holders. As a result, no gain or loss on such changes would be recognised in profit or loss (see paragraph BC4 of the Basis for Conclusions).

Do you agree? If not, why not and what alternative would you propose?

CNC comments

The treatment of changes in the parent's ownership interest in a subsidiary which do not result in a loss of control as "transactions with equity holders" is a consequence of the economic entity approach to consolidation.

Whilst we agree that non-controlling interests are presented in equity we consider they are of a special nature since they represent third party interests in certain subsidiaries. In this respect we concur with the views of dissenting Board members expressed in AV2 that believe that non-controlling interests represent equity claims that are restricted to particular subsidiaries. We question whether it is a necessary consequence that transactions of this kind should not be recognised in profit and loss since the result is attributable to the controlling equity holders.

Due to the concerns expressed about the economic entity, we recommend that this issue should be dealt with by the project "Performance Reporting» and that in the meantime, current requirements should not be changed.

Question 2

Paragraph 30D proposes that on loss of control of a subsidiary any non-controlling equity investment remaining in the former subsidiary should be remeasured to its fair value in the consolidated financial statements at the date control is lost. Paragraph 30C proposes that the gain or loss on such remeasurement be included in the determination of the gain or loss arising on loss of control (see paragraph BC7 of the Basis for Conclusions).

Do you agree that the remaining non-controlling equity investment should be remeasured to fair value in these circumstances? If not, why not and what alternative would you propose?

Do you agree with the proposal to include any gain or loss resulting from such remeasurement in the calculation of the gain or loss arising on loss of control? If not, why not, and what alternative would you propose?

CNC comments

We disagree that the remaining non-controlling interest should be measured at fair value where the residual interest is an associate as defined by IAS 28 or a jointly controlled entity as defined by IAS 31, since the these standards still require that such investments be accounted for at cost at acquisition. We then consider that the argument of the Board in the Basis for Conclusions paragraph 7 and 8 that says that the loss of control is such a significant economic event that justifies the re-measurement of the remaining interest, is not convincing.
We believe that that retained investment does not form part of the exchange transaction and, for that reason, should not be revalued. We also consider that the proposed accounting would lead to recognising through profit or loss, the revaluation of internally generated goodwill which is inconsistent with IAS 38 which clearly precludes such recognition.

Therefore, we strongly recommend to keep existing IAS 27 unchanged on this matter.

Where the residual non controlling interest is classified as "Available for Sale" in accordance with IAS 39 we agree that the application of this standard leads to measuring the investment at fair value. However, present provisions of IAS 39 should also be applied from the date of loss of control and such a re-measurement gain should be accounted for in equity.
The issue of whether the revaluation should be accounted for through equity or through profit and loss is a matter, which should be dealt with in the project "Performance Reporting".

Question 3

As explained in Question 1, the Exposure Draft proposes that changes in a parent's ownership interest in a subsidiary that do not result in a loss of control should be treated as transactions with equity holders in their capacity as equity holders. Therefore, no gain or loss would be recognised in profit or loss.
However, a decrease in the parent's ownership interest resulting in the loss of control of a subsidiary would result in any gain or loss being recognised in profit or loss for the period. The Board is aware that differences in accounting that depend on whether a change in control occurs could create opportunities for entities to structure transactions to achieve a particular accounting result.

To reduce this risk, the Exposure Draft proposes that if one or more of the indicators in paragraph 30F are present, it is presumed that two or more disposal transactions or arrangements that result in a loss of control should be accounted for as a single transaction or arrangement. This presumption can be overcome if the entity can demonstrate clearly that such accounting would be inappropriate (see paragraphs BC9-BC13 of the Basis for Conclusions).

Do you agree that it is appropriate to presume that multiple arrangements that result in a loss of control should be accounted for as a single arrangement when the indicators in paragraph 30F are present? Are the proposed factors suitable indicators? If not, what alternative indicators would you propose?

CNC comments

We agree with the proposals in the Exposure Draft.

Question 4

Paragraph 35 proposes that losses applicable to the non-controlling interest in a subsidiary should be allocated to the non-controlling interest even if such losses exceed the non-controlling interest in the subsidiary's equity. Non-controlling interests are part of the equity of the group and, therefore, participate proportionally in the risks and rewards of investment in the subsidiary.

Do you agree with the proposed loss allocation? Do you agree that any guarantees or other support arrangements from the controlling and non-controlling interests should be accounted for separately? If not, why not, and what alternative treatment would you propose?

CNC comments

We disagree with the proposal and consider the current requirements of IAS 27 appropriate. We consider that allocation of losses to non controlling interests should be mainly based on facts and circumstances, taking into account any contractual agreement relating to such allocation of losses.

Question 5

The transitional provisions in the Exposure Draft propose that all of its requirements should apply retrospectively, except in limited circumstances in which the Board believes that retrospective application is likely to be impracticable.

Do you agree that proposed paragraphs 30A, 30C and 30D should apply on a prospective basis in the cases set out in paragraph 43B? Do you believe that retrospective application is inappropriate for any other proposals addressed by the Exposure Draft? If so, what other proposals do you believe should be applied prospectively and why?

CNC comments

We agree with the proposals in the Exposure Draft as we generally consider retrospective application as preferable but agree with the need for certain practical exceptions such as paragraphs 30 A, 30 C and 30 D.

Other comments

Amendments to IAS 1 *Presentation of Financial statements.*

We disagree with the proposed format of the statement of changes in equity on page 25 of the Exposure Draft. We agree with the paragraph 97 b that such statement should disclose separately for total equity, equity attributable to equity holders of the parent and non-controlling interest a reconciliation of the carrying amount at the beginning and at the end of period. However, we disagree with the change of presentation giving the analysis for major captions of equity for total equity as opposed to equity attributable to holders of the parent only. We believe that the existing format gives information which is far more useful and relevant for the users of financial statements and we do not see the relevance of mixing the analysis of non-controlling interests with that of parent company holders minority interest.

Amendments to IAS 21 *The effects of changes in Foreign Exchange Rate*

We believe that paragraph 48 of the revised IAS 21 is flawed as the sentence "only the proportionate share of the related accumulated foreign exchange difference is recognised in profit loss" seems in total contradiction with paragraph 30 E (c) of the revised IAS 27.

ED OF PROPOSED AMENDMENTS TO
IAS 37 *Provisions, Contingent Liabilities and Contingent Assets and*

Question 1 – Scope of IAS 37 and terminology

The Exposure Draft proposes to clarify that IAS 37, except in specified cases, should be applied in accounting for all non-financial liabilities that are not within the scope of other Standards (see paragraph 2). To emphasise this point, the Exposure Draft does not use ‘provision’ as a defined term to describe liabilities within its scope. Instead, it uses the term ‘non-financial liability’ (see paragraph 10). However, the Exposure Draft explains that an entity may describe some classes of non-financial liabilities as provisions in their financial statements (see paragraph 9).

(a) Do you agree that IAS 37 should be applied in accounting for all non-financial liabilities that are not within the scope of other Standards? If not, for which type of liabilities do you regard its requirements as inappropriate and why?
(b) Do you agree with not using ‘provision’ as a defined term? If not, why not?

CNC comments

(a) The Exposure Draft stipulates that IAS 37 should be applied in accounting for all non-financial liabilities that are not within the scope of other standards and that a non-financial liability is defined as “a liability other than a financial liability as defined in IAS 32”. The exact effect of the proposed scope increase is not evident. Actually, we are unsure of what additional non financial liabilities which were outside the scope of existing IAS 37 would now be covered by the revised standard. In order to clarify the impact of the change, it would be helpful if the IASB provided examples through a list of liabilities not previously covered by the scope of the existing IAS 37 which would be included in the amen
ded version.

We are unsure whether the proposed modifications would lead to include advances/prepayments from customers and deferred revenue. If it was the case, such inclusion would lead to measure that liability at the amount that the entity would rationally pay to settle the obligation or to transfer it to a third party. Nevertheless, at this stage, this seems inconsistent with the fact that the Board just acknowledged that the legal lay off method may not be an appropriate measurement method for revenue recognition.

(b) The term “provision” to indicate a liability of uncertain timing or amount still appears relevant and we therefore recommend that the Board maintain the existing definition. We also note that the Board recognises that an entity may describe some classes of non-financial liabilities as provisions in their financial statements. This would be an additional argument for keeping “provision” as a defined term and not changing its current meaning.

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Question 2 – Contingent liabilities

The Exposure Draft proposes to eliminate the term 'contingent liability'. The Basis for Conclusions on the proposals in the Exposure Draft explains that liabilities arise only from unconditional (or non-contingent) obligations (see paragraph BC11). Hence, it highlights that something that is a liability (an unconditional obligation) cannot be contingent or conditional, and that an obligation that is contingent or conditional on the occurrence or non-occurrence of a future event does not by itself give rise to a liability (see paragraph BC30). The Basis for Conclusions also explains that many items previously described as contingent liabilities satisfy the definition of a liability in the Framework. This is because the contingency does not relate to whether an unconditional obligation exists. Rather it relates to one or more uncertain future events that affect the amount that will be required to settle the unconditional obligation (see paragraph BC23).

The Basis for Conclusions highlights that many items previously described as contingent liabilities can be analysed into two obligations: an unconditional obligation and a conditional obligation. The unconditional obligation establishes the liability and the conditional obligation affects the amount that will be required to settle the liability (see paragraph BC24).
The Exposure Draft proposes that when the amount that will be required to settle a liability (unconditional obligation) is contingent (or conditional) on the occurrence or non-occurrence of one or more uncertain future events, the liability is recognised independently of the probability that the uncertain future event(s) will occur (or fail to occur). Uncertainty about the future event(s) is reflected in the measurement of the liability recognised (see paragraph 23).

(a) Do you agree with eliminating the term 'contingent liability'? If not, why not?
(b) Do you agree that when the amount that will be required to settle a liability (unconditional obligation) is contingent on the occurrence or non-occurrence of one or more uncertain future events, the liability should be recognised independently of the probability that the uncertain future event(s) will occur (or fail to occur)? If not, why not?

CNC comments

(a) We disagree with eliminating the term "contingent liability". Conditional obligations that will not be recognised under the Exposure Draft because they are not attached to unconditional obligations may still require to be defined and to be disclosed in the notes. We consider that such information about significant risks, which do not meet the definition of a liability, is relevant to the decision-making needs of users of the financial statements and therefore should be disclosed in the notes.

(b) We do not agree that when the amount that will be required to settle a liability (unconditional obligation) is contingent on the occurrence or non-occurrence of one or more uncertain future events, the liability should be recognised independently of the probability that the uncertain future event(s) will occur (or fail to occur).

The definition of a liability still includes an "expected outflow of resources". We therefore do not understand how a liability could be recognised independently of the probability that an event will occur resulting in an outflow of resources. This seems also in contradiction with the recognition criteria n the Conceptual framework.

The definition of the triggering event of an unconditional obligation is unclear. For example, we do not see why the obligating event is different between Examples 1 and 2 of the standard. In Example 1 *Disputed lawsuit*, the obligating event is the start of legal proceedings whereas in Example 2 *Potential lawsuit*, it is "an operation in which negligence occurred". Paragraph 13 explains with reference to a present obligation that "the entity must have little, if any, discretion to avoid settling it". We doubt whether the above examples meet this condition, since until the entity has exhausted all the possibilities of appeal in a lawsuit it can still avoid settlement. Without establishing the probability of an outflow of resources it would appear difficult to justify even the existence of a liability in the above examples which are of a "contingent" nature.
This lack of precision constitutes the main weakness of the proposal as the same situation may lead to different accounting. We believe the proposal and guidance must be clear enough to avoid misunderstanding between preparers and to ensure comparability of the financial statements.

Furthermore, the measurement of contingent liabilities (unconditional obligations with a low probability of cash settlement) at fair value has no predictive value for future cash flows. We consider that it is a less relevant and useful information for the users of the financial statements than the one that is based on the best estimate of the amount that an entity would rationally pay to settle the obligation.

The proposed approach is likely to lead to the recognition of an increased population of liabilities with a low probability level of occurrence, therefore increasing materially the cost of producing an information which is not more relevant.

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Question 3 – Contingent assets

The Exposure Draft proposes to eliminate the term 'contingent asset'. As with contingent liabilities, the Basis for Conclusions explains that assets arise only from unconditional (or non-contingent) rights (see paragraph BC11). Hence, an asset (an unconditional right) cannot be contingent or conditional, and a right that is contingent or conditional on the occurrence or non-occurrence of a future event does not by itself give rise to an asset (see paragraph BC17).
The Basis for Conclusions also explains that many items previously described as contingent assets satisfy the definition of an asset in the Framework. This is because the contingency does not relate to whether an unconditional right exists. Rather, it relates to one or more uncertain future events that affect the amount of the future economic benefits embodied in the asset (see paragraph BC17).

The Exposure Draft proposes that items previously described as contingent assets that satisfy the definition of an asset should be within the scope of IAS 38 Intangible Assets rather than IAS 37 (except for rights to reimbursement, which remain within the scope of IAS 37). This is because such items are non-monetary assets without physical substance and, subject to meeting the identifiability criterion in IAS 38, are intangible assets (see paragraph A22 in the Appendix). The Exposure Draft does not propose any amendments to the recognition requirements of IAS 38.

(a) Do you agree with eliminating the term 'contingent asset'? If not, why not?

(b) Do you agree that items previously described as contingent assets that satisfy the definition of an asset should be within the scope of IAS 38? If not, why not?

CNC comments

(a) We consider the concept of a "contingent asset" relevant as a disclosure item where the probability of an economic inflow is insufficient to recognise an asset (see (b) below).

(b) In principle, we agree that contingent assets that meet the definition of an intangible asset should be addressed by IAS 38. We are, however, concerned that the "virtual certainty" recognition condition in §33 of the current IAS 37 is weakened since it is replaced by "probable …expected future economic benefits " in IAS 38.

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Question 4 – Constructive obligations

The Exposure Draft proposes amending the definition of a constructive obligation to emphasise that an entity has a constructive obligation only if its actions result in other parties having a valid expectation on which they can reasonably rely that the entity will perform (see paragraph 10). The Exposure Draft also provides additional guidance for determining whether an entity has incurred a constructive obligation (see paragraph 15).

(a) Do you agree with the proposed amendment to the definition of a constructive obligation? If not, why not? How would you define one and why?

(c) Is the additional guidance for determining whether an entity has incurred a constructive obligation appropriate and helpful? If not, why not? Is it sufficient? If not, what other guidance should be provided?

CNC comments

(a) The amendment to the definition of a constructive obligation (see BC 59) introduces “the notion that the counter party should be reasonably able to rely on the entity to discharge its obligations”. As such, the definition comes closer to but falls short of that of SFAS 143 , which is a legally binding obligation. Indeed we can legitimately query why the Board did not opt directly for the definition of a legally binding obligation as under US GAAP.

The true impact of this change is difficult to measure and further guidance would be appropriate.

(b) The guidance given in §15 is valuable. However, as stated in (a) above we do not believe it goes far enough.

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Question 5 – Probability recognition criterion

The Exposure Draft proposes omitting the probability recognition criterion (currently in paragraph 14(b)) from the Standard because, in all cases, an unconditional obligation satisfies the criterion. Therefore, items that satisfy the definition of a liability are recognised unless they cannot be measured reliably.
The Basis for Conclusions emphasises that the probability recognition criterion is used in the Framework to determine whether it is probable that settlement of an item that has previously been determined to be a liability will require an outflow of economic benefits from the entity. In other words, the Framework requires an entity to determine whether a liability exists before considering whether that liability should be recognised. The Basis notes that in many cases, although there may be uncertainty about the amount and timing of the resources that will be required to settle a liability, there is little or no uncertainty that settlement will require some outflow of resources. An example is an entity that has an obligation to decommission plant or to restore previously contaminated land. The Basis also outlines the Board’s conclusion that in cases previously described as contingent liabilities in which the entity has an unconditional obligation and a conditional obligation, the probability recognition criterion should be applied to the unconditional obligation (i.e. the liability) rather than the conditional obligation.
So, for example, in the case of a product warranty, the question is not whether it is probable that the entity will be required to repair or replace the product. Rather, the question is whether the entity’s unconditional obligation to provide warranty coverage for the duration of the warranty (i.e. to stand ready to honour warranty claims) will probably result in an outflow of economic benefits (see paragraphs BC37-BC41).

The Basis for Conclusions highlights that the Framework articulates the probability recognition criterion in terms of an outflow of economic benefits, not just direct cash flows. This includes the provision of services. An entity’s unconditional obligation to stand ready to honour a conditional obligation if an uncertain future event occurs (or fails to occur) is a type *of service obligation. Therefore, any liability that incorporates an unconditional obligation satisfies the probability recognition criterion. For example, the issuer of a product warranty has a certain (not just probable) outflow of economic benefits because it is providing a service for the duration of the contract, i.e. it is standing ready to honour warranty claims (see paragraphs BC42-BC47).*

Do you agree with the analysis of the probability recognition criterion and, therefore, with the reasons for omitting it from the Standard? If not, how would you apply the probability recognition criterion to examples such as product warranties, written options and other unconditional obligations that incorporate conditional obligations?

CNC comments

We strongly disagree with the proposed amendment as it is inconsistent with the existing recognition criterion in the "Framework". Such inconsistency was highlighted by the Board in paragraph 112 of the Basis for Conclusions of IFRS 3 when applying the provision for recognizing a contingent liability. We are opposed to the fact that the Exposure Draft introduces such a significant conceptual change, which normally should be discussed and addressed in the context of a wide debate on the revision of the "Framework".

At this stage, we do not support the reasoning to consider that there is always an unconditional obligation which meets the recognition criteria of a liability and that the conditional element has only to be taken into account for measurement purposes.

Furthermore we do not believe that the examples given in the ED support the affirmation that "omitting the probability recognition criterion from the Standard because, in all cases, an unconditional obligation satisfies the criterion." We refer to our response on question 2 where we pointed out that the ED does not provide a clear definition of what an unconditional obligation is. Particularly, we agree with the views expressed by the dissenting Board member in AV 2 to 7.

Furthermore, the probability criterion has proven to be a practical basis for both identifying and measuring liabilities and should not be abandoned unless a demonstrably better approach can be proposed.

We wish to underline the objection expressed in AV 4 that the ED does not stipulate what level of uncertainty would preclude recognition particularly because the reliable measurement criteria is not met. As stated in our answer to 2 above there is the danger that the proposed approach will multiply the liabilities recognised by including items of remote probability that would not meet the definition of a liability in the current "Framework".

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Question 6 – Measurement

The Exposure Draft proposes that an entity should measure a non-financial liability at the amount that it would rationally pay to settle the present obligation or to transfer it to a third party on the balance sheet date (see paragraph 29).
The Exposure Draft explains that an expected cash flow approach is an appropriate basis for measuring a non-financial liability for both a class of similar obligations and a single obligation. It highlights that measuring a single obligation at the most likely outcome would not necessarily be consistent with the Standard's measurement objective (see paragraph 31).

Do you agree with the proposed amendments to the measurement requirements? If not, why not? What measurement would you propose and why?

CNC comments

We are opposed to the proposed amendments to the measurement requirements. In particular, we do not support the "legal lay-off" method as a way to measure single liabilities because (i) the absence of an active market will often prevent implementation (non reliable measurement) and (ii) the valuation of the liability will include the margin of the intermediary that takes it over.

The Board has already recognised the practical difficulties of the "legal lay-off" method with respect to the Revenue Recognition project and we are not convinced that these difficulties have now disappeared.

The "probable outcome" principle in the existing standard provides a practical and pragmatic approach to the measurement of single liabilities and the statistically probable outcome can be applied to a class of liabilities e.g. warranty claims. We have not seen arguments or evidence in the Exposure Draft to demonstrate that the proposed "cash flow" approach will produce better results for a single liability.

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Question 7 – Reimbursements

The Exposure Draft proposes that when an entity has a right to reimbursement for some or all of the economic benefits that will be required to settle a non-financial liability, it recognises the reimbursement right as an asset if the reimbursement right can be measured reliably (see paragraph 46).

Do you agree with the proposed amendment to the recognition requirements for reimbursements? If not, why not? What recognition requirements would you propose and why?

CNC comments

We do not agree with the proposed recognition requirements for reimbursements. We do not believe that a reimbursement (which remains within the scope of IAS 37) should be recognised as an asset on the only basis that it can be measured reliably. Under the current version of IAS 37 "the reimbursement shall be recognised when, and only when, it is virtually certain that reimbursement will be received." We believe that the above recognition criterion is still relevant and should be carried forward or, at least, that it should be consistent with the existing "Framework", and include at a minimum the probability that the reimbursement will be received.

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Question 8 – Onerous contracts

The Exposure Draft proposes that if a contract will become onerous as a result of an entity's own action, the liability should not be recognised until the entity takes that action. Hence, in the case of a property held under an operating lease that becomes onerous as a result of the entity's actions (for example, as a result of a restructuring) the liability is recognised when the entity ceases to use the property (see paragraphs 55 and 57). In addition, the Exposure Draft proposes that, if the onerous contract is an operating lease, the unavoidable cost of the contract is the remaining lease commitment reduced by the estimated sublease rentals that the entity could reasonably obtain, regardless of whether the entity intends to enter into a sublease (see paragraph 58).

(a) Do you agree with the proposed amendment that a liability for a contract that becomes onerous as a result of the entity's own actions should be recognised only when the entity has taken that action? If not, when should it be recognised and why?

(b) Do you agree with the additional guidance for clarifying the measurement of a liability for an onerous operating lease? If not, why not? How would you measure the liability?

(c) If you do not agree, would you be prepared to accept the amendments to achieve convergence?

CNC comments

(a) We agree with the proposed amendment.

(b) We are not sure we fully understand the proposed guidance which should be clarified. We clearly do not agree with the proposed amendment if the intention of the Board in paragraph 57 is to require the recognition of a liability for an operating lease (other than when accounting for a business combination) only on the basis that, because of changes in the market, the lease rent becomes higher that the market rent.

Recognizing a loss in such circumstances would not be consistent with the accounting in cases where the leased asset is recognized in the balance sheet.

(c) Not applicable.

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Question 9 – Restructuring provisions

The Exposure Draft proposes that non-financial liabilities for costs associated with a restructuring should be recognised on the same basis as if they arose independently of a restructuring, namely when the entity has a liability for those costs (see paragraphs 61 and 62).
The Exposure Draft proposes guidance (or provides cross-references to other Standards) for applying this principle to two types of costs that are often associated with a restructuring: termination benefits and contract termination costs (see paragraphs 63 and 64).

(a) Do you agree that a liability for each cost associated with a restructuring should be recognised when the entity has a liability for that cost, in contrast to the current approach of recognising at a specified point a single liability for all of the costs associated with the restructuring? If not, why not?

(b) Is the guidance for applying the Standard's principles to costs associated with a restructuring appropriate? If not, why not? Is it sufficient? If not, what other guidance should be added?

CNC comments

(a) We do not agree with the proposed amendment as we support the current approach of recognising at a specific point a single liability for all costs associated with the restructuring where the latter clearly form part of a single plan.

In this case, recognising of the total cost and liability of the restructuring plan better reflects the economic substance of the transaction and gives a more relevant information to users of the financial statements. If each cost is recognised separately when the entity has a liability in accordance with each appropriate standard, there is likely to be a dilution of this information as the relevant costs may be recognised in different accounting periods. (see our comments on question IAS 19 – 2B)

(b) It appears appropriate.

ED OF PROPOSED AMENDMENTS TO
IAS 19 *Employee Benefits*

Question 1 – Definition of termination benefits

The Exposure Draft proposes amending the definition of termination benefits to clarify that benefits that are offered in exchange for an employee's decision to accept voluntary termination of employment are termination benefits only if they are offered for a short period (see paragraph 7). Other employee benefits that are offered to encourage employees to leave service before normal retirement date are post-employment benefits (see paragraph 135).

Do you agree with this amendment? If not, how would you characterise such benefits, and why?

CNC comments

We agree with the amended definition as it clarifies the distinction between termination and post-employment benefits.

We would however appreciate additional guidance to explain what is meant by "offered for a short period". We wonder what short means in terms of duration. Moreover, we question whether it is the exceptional "one-off" nature rather than the duration which is important. For example, where offers are repeated frequently for a short period would the definition of a termination benefit be met?

In the proposed definition in paragraph 7(a), involuntary termination benefits are defined as benefits provided before the normal retirement date. The definition in 7(b) of voluntary termination benefits does not mention that they are granted before the normal retirement date. On the contrary, the first sentence of the new paragraph 135 and the question 1 refer to involuntary termination benefits as benefits obtained before normal retirement date. We think that the definition in paragraph 7 should make clear that both involuntary and voluntary benefits are paid before the normal retirement date.

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Question 2 – Recognition of termination benefits

The Exposure Draft proposes that voluntary termination benefits should be recognised when employees accept the entity's offer of those benefits (see paragraph 137). It also proposes that involuntary termination benefits, with the exception of those provided in exchange for employees' future services, should be recognised when the entity has communicated its plan of termination to the affected employees and the plan meets specified criteria (see paragraph 138).

Is recognition of a liability for voluntary and involuntary termination benefits at these points appropriate? If not, when should they be recognised and why?

CNC comments

Voluntary termination benefits

The proposed recognition criterion for voluntary termination benefits appears inconsistent with the "unconditional obligation" concept for recognising liabilities under the ED of IAS 37.

Paragraph BC 18 of the Basis for Conclusions justifies employee acceptance as a recognition criterion since before acceptance "the entity would typically have the discretion to withdraw the offer and, therefore, have no present obligation". This explanation appears to ignore the practical and legal difficulties associated with withdrawing a published offer in certain countries. We would argue that in practice the entity is already committed by the publication of an offer and should "stand ready " to honour its obligation if the employees accept the offer.

Furthermore, voluntary and involuntary benefits will often be part of the same restructuring plan. They would be communicated simultaneously and negotiated as a "package" with union representatives. In this case, they would in substance be part of the same transaction. As a result, a common recognition criterion would give more relevant information on the financial impact of the restructuring or termination plan.

Involuntary termination benefits

We agree with the proposed recognition criteria for involuntary termination benefits and suggest that the same criteria could be applied to voluntary benefits especially when they are part of one social plan.

With respect to the condition that the "entity has communicated its plan of termination to the affected employees" we would add that the communication to official employee representatives also fulfils this condition.

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Question 3 – Recognition of involuntary termination benefits that relate to future service

The Exposure Draft proposes that if involuntary termination benefits are provided in exchange for employees' future services, the liability for those benefits should be recognised over the period of the future service (see paragraph 139).

The Exposure Draft proposes three criteria for determining whether involuntary termination benefits are provided in exchange for future services (see paragraph 140).

Do you agree with the criteria for determining whether involuntary termination benefits are provided in exchange for future services? If not, why not and what criteria would you propose? In these cases, is recognition of a liability over the future service period appropriate? If not, when should it be recognised and why?

CNC comments

We agree with the criteria for determining whether involuntary termination benefits are provided in exchange for future services.

However, we wonder why the proposed amendment does not address the case where voluntary termination benefits would be provided in exchange for future services.

Paragraph 137 stipulates that when the employee accepts the employer's offer a liability and an equivalent expense for voluntary termination is recognised. No exception is introduced for voluntary termination benefits provided in exchange for future services. We see no reason in substance for treating voluntary and involuntary benefits differently.

Additional comments

1. **The standard should indicate the required accounting for benefits plans which authorize the employee to reduce its working hours until normal retirement age with a less than proportional salary decrease. These benefits are granted up to the normal retirement age and therefore cannot qualify as termination benefits.**