

XX January 2008

International Accounting Standards Board
30 Cannon Street
London
EC4M 6XH
United Kingdom

DRAFT COMMENT LETTER

Comments should be sent to Commentletter@efrag.org by 17 January 2009

Dear Madam/Sir

Exposure Draft of proposed amendments to IFRS 5 *Discontinued Operations*

On behalf of the European Financial Reporting Advisory Group (EFRAG) I am writing to comment on the Exposure Draft of proposed amendments to IFRS 5 *Discontinued Operations* (the ED). This letter is submitted in EFRAG's capacity of contributing to IASB's due process and does not necessarily indicate the conclusions that would be reached in its capacity of advising the European Commission on endorsement of the definitive interpretations/amendments on the issues.

The ED proposes to introduce a new, converged definition of 'discontinued operations'. It also proposes to require additional disclosures related to components of an entity that have been or will be disposed of; and the intention is that those disclosures will be common to both IFRS and US GAAP.

Although EFRAG is broadly supportive of the IASB's efforts to achieve greater convergence in this area, it has some significant concerns about the detailed proposals. In particular:

- Although EFRAG is supportive of basing the definition of a discontinued operation on IFRS 8's notion of operating segments, we are not sure whether the IASB's objective for this ED (the separate presentation of all strategic shifts) will be met in all cases by doing so.
- EFRAG does not support the proposal that information about all components of the reporting entity that have been either disposed of or are classified as held for sale should be disclosed, regardless whether those components are a discontinued operation as defined. We think the proposal mixes two alternative approaches, and will also result in too many small discontinuances being disclosed in the notes.

Our detailed comments are set out in the appendix to this letter.

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We hope that you find our comments helpful. If you wish to discuss them further, please do not hesitate to contact Frederiek Vermeulen or me.

Yours sincerely

Stig Enevoldsen
EFRAG, Chairman

Appendix

EFRAF's detailed comments on the ED *Discontinued Operations*

Question 1 – Definition of discontinued operations

IFRS 5 defines a discontinued operation as a component of an entity that either has been disposed of or is classified as held for sale and

- (a) represents a separate major line of business or geographical area of operations,*
- (b) is part of a single co-ordinated plan to dispose of a separate major line of business or geographical area of operations, or*
- (c) is a subsidiary acquired exclusively with a view to resale.*

This exposure draft proposes changing the definition so that a discontinued operation is a component of an entity that

- (a) is an operating segment (as that term is defined in IFRS 8 Segment Reporting) and either has been disposed of or is classified as held for sale or*
- (b) is a business (as that term is defined in IFRS 3 Business Combinations (as revised in 2008)) that meets the criteria to be classified as held for sale on acquisition.*

The exposure draft proposes that an entity should determine whether the component of an entity meets the definition of an operating segment regardless of whether it is required to apply IFRS 8.

Question 1(a)—Do you agree with the proposed definition? Why or why not? If not, what definition would you propose, and why?

- 1 As a general comment, EFRAG is broadly supportive of the efforts of the IASB and FASB to achieve greater convergence between IFRS and US GAAP—because we believe it will benefit global accounting—as long as that convergence is not pursued regardless of cost. In particular, we have to date supported the Boards' efforts to achieve greater convergence in the area of accounting for discontinued operations, and we think an important part of that process is to have a converged definition of a discontinued operation.
- 2 We agree that it is logical to focus the approach to discontinued operations on operating segments, as defined in IFRS 8; if a component of the business is considered important enough to deal with separately in the segment reporting when it is a continuing operation, it should be important enough to deal with separately when it is a discontinued operation and if it is *not* important enough to deal with separately in the segment reporting when it is a continuing operation, it is also not important enough to deal with separately when it is a discontinued operation.
- 3 However, we note from the Introduction and Basis for Conclusions of the ED that the objective of the proposed amendments is to require a disposal activity to be "presented as a discontinued operation only when an entity has made a strategic shift in its operations" and have debated at some length whether 'a strategic shift' and 'discontinuing an IFRS 8 operating segment' will in all cases be the same thing. For

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example, consider the position of a company that has various product lines and operates in various countries and provides segment information by product line. It decides to close down its operations in a particular country. As that is not a reported segment, it would under the ED not be treated as a discontinued operation. EFRAG members are in two minds as to whether this could be regarded as a strategic shift.

- 4 To avoid this confusion, we suggest removing all references to 'strategic shifts' and, using the reasoning set out at the end of paragraph 3 above, focus instead exclusively on the operating segment notion. We note however that this would still mean that, in our example, closure of the entity's operations in a particular country would not be presented separately.
- 5 On a more detailed level, we suggest that the way in which subparagraph (b) of the definition is worded should be looked at again, because we stumbled over it. An amendment along the following lines might help:

(b) is a *business* that on acquisition met ~~meets~~ the criteria to be classified as held for sale ~~on acquisition~~.

- 6 In addition, we think that the IASB should clarify whether the references to 'operating segments' are references to operating segments prior to aggregation or after aggregation. We think it would be consistent with the proposed amendment to IAS 36 being made as part of the Improvements to IFRSs (2008) (Impairment of Assets – unit of accounting for goodwill impairment) were the reference be to operating segments before aggregation. We also think that is what the ED implies by referring in paragraph 32 to paragraphs 5-10 of IFRS 8, but we think it would be helpful if explicit guidance was provided.

Question 1(b)—If an entity is not required to apply IFRS 8, is it feasible for the entity to determine whether the component of an entity meets the definition of an operating segment? Why or why not? If not, what definition would you propose for an entity that is not required to apply IFRS 8, and why?

- 7 EFRAG sees no difficulty in entities that are not required to apply IFRS 8 being required to apply an operating segment notion when applying IFRS 5. The operating segment notion refers to the reporting entity's internal reporting system—not to whether or not it was listed—and it would have an internal reporting system regardless of whether the entity is applying IFRS 8.

Question to constituents

- 8 EFRAG has discussed at some length whether, if it is not considered useful for an entity to provide information about its continuing segments (in other words, if it is not necessary for it to comply with IFRS 8), why it should be considered useful for it to provide information about discontinued segments. We would particularly welcome your views on this issue.

Question 2 – Amounts presented for discontinued operations

Under IFRS 8, amounts disclosed for operating segments are the amounts reported to the chief operating decision maker. Nevertheless, although the proposed definition of a discontinued operation refers to operating segments, this exposure draft proposes that the amounts presented for discontinued operations should be based on the amounts presented in the statement of comprehensive income, even if segment information disclosed to comply with IFRS 8 includes different amounts that are reported to the chief operating decision maker.

Question 2—Do you agree that the amounts presented for discontinued operations should be based on the amounts presented in the statement of comprehensive income? Why or why not? If not, what amounts should be presented and why?

- 9 EFRAG agrees that, in order to present objective and consistent data, amounts should be determined in accordance with those IFRSs used to determine the amounts presented in the statement of comprehensive income.

Question 3 – Disclosures for all components of an entity that have been disposed of or are classified as held for sale

The exposure draft proposes disclosures for all components of an entity that have been disposed of or are classified as held for sale, except for businesses that meet the criteria to be classified as held for sale on acquisition.

Question 3(a)—Do you agree with the proposed disclosure requirements? Why, or why not? If not, what changes would you propose, and why?

The scope of proposed new paragraph 41A

- 10 We do not support the approach proposed in paragraph 41A, which is that information about components of the reporting entity that have been either disposed of or are classified as held for sale should be provided in the notes of the financial statements, regardless of whether those components are a discontinued operation as defined.
- 11 In our view, the principal objective of this disclosure should be to support the income statement presentation by providing more information about the discontinuances presented separately in that statement. We think that a disclosure that focuses on components that have either been disposed of or classified as held for sale—where a component might be an operating segment but also might not be (or could be smaller, or simply different)—does not do that. In addition we think that this component notion could require very small discontinuances to be disclosed, which we think would result in clutter rather than useful information. Finally, we have some concerns as to whether the information necessary to comply with the proposed disclosure would always be available (particularly for the corresponding periods).
- 12 In addition, we are very uncomfortable with the rationale for this disclosure requirement, as set out in paragraph BC8. That rationale is in effect that the IASB and FASB could not agree on how to define a discontinued operation, with FASB favouring a definition that would treat smaller components of the entity as discontinued operations than the definition the IASB favoured; so a compromise was reached in which the IASB got its way on the definition of a discontinued operation, but disclosures would be required that would ensure that the information that FASB thought should be disclosed on the

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face of the primary financial statements would at least be disclosed in the notes. We understand that, if convergence is to be achieved, compromise will sometimes be necessary. However, it seems to us that the approach adopted in paragraph 41A is inconsistent with the philosophy behind the other changes being proposed; which is that (i) if a component of the business is considered important enough to deal with separately in the notes when it is a continuing operation, it should be important enough to deal with separately when it is a discontinued operation and (ii) if it is *not* important enough to deal with separately in the notes when it is a continuing operation, it is also not important enough to deal with separately when it is a discontinued operation.

Question for constituents

EFRAG debated this issue at some length with some members believing that the notes should deal only with discontinuances presented separately in the income statement and others believing that the notes should also deal with smaller discontinuances. Some EFRAG members favoured that second approach, believing that what users want is information about material discontinuances, of which only the largest will be dealt with by separate presentation. However, the approach proposed by the IASB is neither of those approaches, and is thus in EFRAG's view not compatible with the approach adopted in the income statement.

EFRAG also noted that a 'component' as described in the ED could be very small. EFRAG thinks that, in addition to the clutter this might cause, it could also result in some unhelpful disclosures; for example, a company that closes three shops and open three new shops nearby could be required to provide the disclosures about the three shops closed but not about the ones opened. This is not helpful disclosure.

EFRAG would particularly welcome constituent's views on these issues.

Subsuming existing paragraphs 33(c) and (d) into proposed new paragraph 41A

- 13 We note that the disclosure requirements that are in paragraphs 33(c) and (d) of the existing standard have been "subsumed" into paragraphs 41A(c) and (b). This is of course not simply about moving a requirement around within the standard, because paragraph 33 applies only to discontinued operations whilst paragraph 41A applies to all discontinued components. We have tried to understand the rationale for this change and can only presume that it is part of the compromise reached with FASB mentioned earlier.
- 14 EFRAG commented in the previous section of its response to question 3(a) that it thinks that proposed new paragraph 41A's disclosure would cover too many discontinuances. We suggest that the scope of proposed new paragraph 41A should be narrowed.
 - (a) If that is done in the way that we have suggested, the disclosures required by existing paragraph 33 and by proposed new paragraph 41A will both be provided only for discontinuances that are presented separately in the income statement. As such, we do not think that anything would be achieved by subsuming paragraphs 33(c) and (d) into paragraph 41A.; on the other hand, it would also not cause any harm.

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- (b) On the other hand, if the IASB does not narrow the scope of proposed new paragraph 41A in the way we have suggested, we do not think it is appropriate to subsume paragraphs 33(c) and (d) into paragraph 41A. In our view the disclosures required by existing paragraph 33 should be provided only for discontinuances that are presented separately in the income statement.

Question 3(b)—Do you agree with the disclosure exemptions for businesses that meet the criteria to be classified as held for sale on acquisition? Why or why not? If not, what changes would you propose, and why?

- 15 EFRAG agrees with the proposal in paragraph 41B of the ED to exempt businesses classified on acquisition as held for resale from the disclosures described in paragraph 41A of the ED. The objective of IFRS 5 is to provide users with information about components that have been part of the reporting entity's continuing operations but either no longer are or are expected not to be shortly. Businesses classified on acquisition as held for resale are never part of the entity's continuing operations.

Question 4 – Effective date and transition

Entities would be required to apply the proposed changes prospectively, from a date to be determined by the IASB after exposure, with one exception: the amounts in the statement of comprehensive income (or in the separate income statement) should be reclassified on the basis of the revised definition of discontinued operations for all periods presented. Earlier application would be permitted.

Question 4—Are the transitional provisions appropriate? Why or why not? If not, what would you propose, and why?

- 16 EFRAG's strong preference is that all new or amended accounting requirements should be applied retrospectively, because such application significantly enhances the comparability of the information provided. In our view, if it is difficult to apply a standard in the near-term retrospectively, it is better to allow a longer lead-time that would enable retrospective application than to require (or permit) prospective application. New or amended requirements should be applied prospectively only if retrospective application is impracticable. For those reasons:
 - (a) we welcome the proposal that the changes to the definition of a discontinued operation set out in the ED should be applied retrospectively.
 - (b) we agree with the prospective application of the proposed amendment to the disclosure requirement, because the information might not be available on a retrospective basis. However, if the Board accepts the suggestion we have made to narrow the scope of the proposed new paragraph 41A disclosures, we think it might be possible to apply the amended disclosure requirements retrospectively.