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Mr Robert Garnett
Chairman
The International Financial Reporting
Interpretations Committee of the
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30 Cannon Street
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Our ref MT/288
Contact Mary Tokar

25 April 2008

Dear Mr Garnett

IFRIC Draft Interpretation D23 *Distributions of Non-cash Assets to Owners*

We appreciate the opportunity to comment on the International Financial Reporting Interpretations Committee's (IFRIC) Draft Interpretation D23 *Distributions of Non-cash Assets to Owners*. This letter expresses the views of the international network of KPMG member firms.

We believe that the accounting for non-cash assets to owners in their capacity as owners is an area with diversity in practice for which agreed principles should be developed. However, we do not support the IFRIC's proposals and we recommend that the IFRIC discontinue this project. Instead, we believe that the International Accounting Standards Board (the Board) should deal with the project as part of its existing common control project; there also is a link to the reporting entity phase of the Board's conceptual framework project.

We understand that the Board's project on common control transactions will include consideration of the appropriate accounting for spin-offs (demergers). We believe that this project will need to include the development of a robust concept of when a transaction is with a shareholder, with the entity itself and when it is a third party transaction, and the appropriate measurement attribute(s) for each; this also links to the Board's reporting entity project. In our view, the issues considered in developing such a concept should provide the framework for determining the appropriate accounting for the non-cash distributions that are within the scope of this draft Interpretation.

Additionally, our discussions have led us to believe that the draft Interpretation is overly mechanical and drives the accounting via an artificial focus on the dividend payable. As explained in more detail in our response to Question 1, we believe that a similar problem ultimately led to the withdrawal of IFRIC 3 *Emission Rights*. This further supports the issue being considered at Board level.

Although the common control project will not be completed within the time that it would take for an IFRIC Interpretation to be completed, we believe that two accounting methods applied in



practice currently, the book value method and the fair value method, are acceptable approaches. As explained in our response to Question 1, if we were asked to support a single method, then it would be the book value method.

Appendix 1 to this letter contains our responses to the specific questions asked by the IFRIC.

Please contact Julie Santoro or Mary Tokar at +44 (0)20 7694 8871 if you wish to discuss any of the issues raised in this letter.

Yours sincerely

KPMG IFRG Limited

KPMG IFRG Limited

cc Andrew Vials

Appendix 1

Question 1: Specifying how an entity should measure a liability for a dividend payable

As noted in our covering letter, we believe that the IFRIC should discontinue the project, and that the Board should deal with non-cash distributions to owners as part of its existing common control project. However, if the IFRIC proceeds with the draft Interpretation, then we believe that the proposals should be modified for the reasons outlined below.

BC19 of the proposals states the IFRIC's view that it would *not* be appropriate to measure the dividend payable at the carrying amount of the assets to be distributed. Effectively what is happening is that an entity is settling an obligation with assets in its financial statements. In this context we do not agree that IAS 37 *Provisions, Contingent Liabilities and Contingent Assets* prohibits a carrying amount approach. Paragraph 37 of IAS 37 refers to the best estimate of a provision being the amount that an entity rationally would pay to settle the obligation or to transfer it to a third party; however, some of the specific application guidance in IAS 37 (e.g., the warranty example following paragraph 39, onerous contracts in paragraph 68, and restructuring expenditure in paragraph 80) emphasises direct, incremental costs as the appropriate measurement basis. As discussed during the IASB's round table on possible revisions to IAS 37 in late 2006, the measurement of provisions that an entity will settle itself has focused on cost as the appropriate measurement basis. Accordingly, we believe that the book value method can be supported in accounting for non-cash distributions to owners under IFRSs, at least until the revisions of IAS 37 are finalised.

Looking at the overall effect of the proposals, the IFRIC has concluded that a distribution is a remeasurement event. However, this principle is not established in current IFRSs, and we do not believe that it is clear from the Board's deliberations to date as part of its liabilities project.

We believe that there are similarities between the measurement proposals contained in this draft Interpretation and the measurement requirements of IFRIC 3, which subsequently was withdrawn by the IASB. IFRIC 3 required, and the draft Interpretation proposes, measuring liabilities at fair value even if they will be satisfied with an entity's own assets, rather than at the carrying amount of the assets being used to settle the obligation. This gives rise to an accounting measurement mismatch. The failure of the IFRIC's project on emissions rights suggests a need for a more comprehensive consideration of non-cash distributions to owners, and supports the view that the IFRIC cannot rule out the book value method.

We also have considered whether the requirement in paragraph 34(d) of IAS 27 (2008) *Consolidated and Separate Financial Statements* to measure at fair value any interest retained in a former subsidiary at the date that control is lost should lead automatically to the conclusion that distributions of non-cash assets to owners should be measured at fair value. However, we understand that the Board itself was unable to reach a conclusion on the appropriate measurement attribute in accounting for spin-offs, and that they did not find the change in IAS 27 determinative; this led to paragraph 34(c)(ii) of the standard not specifying the

measurement attribute for such a distribution. Accordingly, we believe that the book value method is not inconsistent with IAS 27 (2008).

In response to the creditors' perspective argument in BC19 for measuring the dividend payable at fair value, in our experience, creditors are more interested in the value of the assets and liabilities retained in the business than those that are no longer within the control of the business. Since there is no requirement for the assets and liabilities retained in the business to be measured at fair value, we do not support the proposal to measure at fair value assets leaving the business via a distribution.

Taking into account the above arguments, if we were asked to support a single method, then it would be the book value method, which we believe is predominant in practice. However, we also recognise the limited practice of fair value measurement for such distributions, and believe that in advance of a broader project it would be inappropriate to preclude this alternative.

Question 2: Specifying how any difference between the carrying amount of the assets distributed and the carrying amount of the dividend payable should be accounted for when an entity settles the dividend payable

As noted in our covering letter, we believe that the IFRIC should discontinue the project, and that the Board should deal with non-cash distributions to owners as part of its existing common control project. If the IFRIC proceeds with the project, then we believe that both the fair value method and the book value method should be identified as acceptable alternatives; see our response to Question 1.

Within the context of the fair value method, we support recognising any difference between the carrying amount of the assets distributed and the carrying amount of the dividend payable in profit or loss. Our reasons for supporting this treatment are consistent with the arguments put forward in BC34-38 of the draft Interpretation.

Question 3: Whether an entity should apply the requirements in IFRS 5 to non-current assets held for distribution to owners

We agree that IFRS 5 *Non-current Assets Held for Sale and Discontinued Operations* should be amended to include within its scope non-current assets held for distribution to owners.

In applying the requirements of IFRS 5, we believe that the criteria in paragraphs 7-9 of the standard in respect of sales transactions should apply equally to a distribution. Therefore the underlying assets would be classified as held for distribution when:

- the assets are available for immediate distribution in their present condition; and

- the distribution is highly probable, i.e.:
 - the appropriate level of management is committed to a plan to make the distribution; and
 - the distribution is expected to occur within one year from the date of classification, with a longer period accepted subject to paragraph 9 of IFRS 5.

Similar to the sale of significant non-current assets (disposal groups), for some entities the distribution of significant non-current assets (disposal groups) may be subject to shareholder approval. In our view, the requirement to obtain shareholder approval does not necessarily mean that the criteria for classification as held for distribution are met only when shareholder approval is obtained. However, if substantive shareholder approval for a distribution is required, then the distribution might not be “highly probable” until shareholder approval is obtained as the need to obtain shareholder approval in such a situation may be considered a significant hurdle.

BC48 of the draft Interpretation states that under current IFRS 5 a non-current asset is classified as held for sale when “the sale is highly probable and the entity is *committed* to a plan to sell”. We believe that this does not reflect accurately the current requirements of IFRS 5. The criteria in paragraphs 7 to 9 of that standard require that (1) the asset must be available for immediate sale in its present condition; and (2) its sale must be highly probable, which means in part that the appropriate level of *management* (rather than the entity) must be committed to a plan to sell the asset. Our response to this question reflects our reading of IFRS 5, including our view on when non-current assets are classified as held for sale in the event that shareholder approval for the disposal is required, rather than simply choosing generically between commitment date and the date at which an obligation arises.