Organismo Italiano di Contabilità – OIC (The Italian Standard Setter)
Italy, 00187 Roma, Via Poli 29
Tel. 0039/06/6976681 fax 0039/06/69766830
e-mail: presidenza@fondazioneoic.it

Mr. Reinhard Biebel
Project Manager EFRAG
Avenue des Arts 41
B -1040 Brussels

5 July 2004

Re : ED Proposed Amendments to IFRS 3 Business Combinations: *Combinations by Contract Alone or Involving Mutual Entities.*

Dear Mr. Biebel,

We are pleased to provide our comments on ED Proposed Amendments to IFRS 3 Business Combinations: *Combinations by Contract Alone or Involving Mutual Entities.*

Yours sincerely

Prof. Angelo Provasoli
(OIC – Chairman)

DRAFT LETTER BY OIC ON IFRS 3

OIC considers IFRS 3 a significant improvement over the now superseded IAS 22 and also an important steps towards convergence with USA gaaps.

However we continue to have a strong concerns on some matters already raised in our comment letter of March 4, 2003 on ED3. We are therefore extremely disappointed that our proposals for changes have not been accepted by the Board.

We refer particularly to the recognition of contingent liabilities of the acquiree as part of allocating the cost of a business combination. We reiterate that this recognition is inconsistent with IAS 37 and with the Framework. It is inconsistent also with the fact that contingent assets of the acquiree are not taken into account. While we are of the opinion that contingent assets should not be part of the allocation exercise we nevertheless note the inconsistency with contingent liabilities and such inconsistency has no justifiable reason.

We are also disappointed with the provision that negative goodwill should always be recognised to profit and loss. We continue to believe that when negative goodwill is a “premium” against future losses, this negative goodwill should be deferred to offset expected losses when these materialize.

In our comment letter to ED3 we also suggested to consider amortization of goodwill in those circumstances where future cash flows cannot be reliably determined. Our suggestion, which we still believe appropriate, has not been accepted by the Board.

We also had a suggestion to consider time value (i.e. discounting) deferred taxes in those cases where it is possible to reasonably estimate timing of reversal and to amend IAS 12 accordingly. Our suggestion, regrettably not accepted, would have avoided a mismatch in measurement whereby assets and liabilities assumed in a business combination are measured taking into account time value but the related tax effect does not take into account time value.

The above comments denote a number of disagreement with IFRS 3 as promulgated but considering that it is nonetheless an improvement over IAS 22, we recommend its adoption by Efrag. We however urge the Board to reconsider our comments above in future so that the Board can correct what we consider intellectual mistakes.

We also urge the Board to complete Phase II of the project on Business Combination given the importance of the subject.