AFM

Thematic Review – Business Combinations (IFRS 3R)

Supervision of Financial Reporting

October 2011

Table of Contents

1 Conclusion and summary 4

2 Introduction 7

3 Objectives of the thematic review, design and population 9

4 Findings 11

Disclaimer

This is an English translation of the original Dutch text, furnished for convenience only. In case of any conflict between this translation and the original text, the latter shall prevail.

1 Conclusion and summary

To a large extent, listed companies have been successful in providing fully adequate disclosure of the effects of business combinations to users of the financial statements. These effects are made visible by applying the standards regarding the treatment of business combinations. This is shown by the thematic review of Business Combinations conducted by the Netherlands Authority for the Financial Markets (AFM) on the financial reporting for 2010. The AFM identifies further improvement, elaboration or clarification in connection with the treatment of business combinations in the following respects:

- Disclosure of the consideration transferred and of each major class of consideration (see 4.3);
- Full disclosure of the contingent consideration arrangements for the acquisition, and any effect on the result for the financial year (see 4.3 and 4.10);
- Disclosure of the amounts recognised on the acquisition date for each category of assets acquired and liabilities assumed, including the accounts receivable acquired (see 4.4);
- Disclosure of the recognition of existing non-controlling equity interests at the time of entering into the business combination (see 4.7);
- Disclosure of acquisition-related costs (see 4.8); and
- Reconsideration of the method of identification of: assumed contingent liabilities and reacquired assets (see 4.4 and 4.5).

General

The standard for business combinations (IFRS 3R) amended in 2008 is also intended to improve the relevance, reliability and comparability of the information provided by a company regarding a business combination and the effects thereof. Companies must apply the changes to this standard in their reporting for financial years beginning on or after 1 July 2009. The changes affect the way in which companies report business combinations. The implementation of changes to a standard is difficult, and it usually takes some time before new best practices are established.

18 percent of listed companies acquired one or more other companies during the 2010 financial year. An acquisition or business combination is an event that increases the amount of information required by users of the financial statements. The AFM investigated how these companies have complied with the standard for business combinations in their financial statements for 2010.

Since the AFM has to conduct its thematic review on the basis of public information[1], it is not able to establish the background to some of its findings. After publication of the report on its thematic review, the AFM will further investigate the financial reporting of the companies concerned and may approach these companies with a request for further information.

---

[1] *Based on Section 2(1) of the Financial Reporting Supervision Act (Wtfv), the AFM can request further disclosure if, on the basis of publicly available facts or circumstances, it has doubts regarding the correct application of the reporting regulations.*

Disclosure of the business combination

A large majority of the companies reviewed include the mandatory disclosure regarding business combinations. The acquiring party (the 'acquirer') must provide information that enables users of the financial statements to assess the nature and financial consequences of a business combination. A majority of the companies state the name of the acquired company (the 'acquiree'), the percentage of the control obtained, a description of the acquiree, the date of the acquisition and how control was obtained. In addition, companies voluntarily report the name of the company and the acquisition date for individual business combinations that were not of material significance. This suggests that companies are taking into account the wishes of the users of financial statements who consider this information to be important.

A large majority of the companies additionally report the revenue and the result of the business combination since the acquisition date. This disclosure helps users to distinguish between autonomous and purchased growth of the company.

In a large majority of cases, the fair value of the consideration transferred is clearly stated. Approximately a quarter of the companies disclose that the consideration transferred includes a contingent consideration. Changes in the value of these contingent liabilities must be recognised in profit or loss, and therefore can affect future financial statements. None of the companies concerned include all the mandatory disclosures regarding contingent considerations. There is thus still room for improvement here.

Allocation to acquired assets and assumed liabilities

Three-quarters of the companies disclose the amounts recognised on the acquisition date for each category of acquired assets and assumed liabilities. With regard to individual items, the picture is more complex. Three-quarters of the companies disclose the goodwill or badwill for each acquisition, and cite synergy and the experience of employees as the most important factors. A good majority of the companies report the fair value of the receivables acquired, but only a small group include all the mandatory disclosures for this item. It is notable that only a very small group of companies provide information on the assumed contingent liabilities. Given the importance of these items for users of the financial statements, the AFM considers that the financial reporting can be improved in these respects.

Three-quarters of the companies identify and measure one or more intangible non-current asset, most commonly concerning items relating to customers and brands. Approximately half of the companies disclose the reason for the acquisition. In virtually all cases, the reason disclosed relates to the intangible non-current asset that is presented. None of the companies reviewed identify an intangible non-current asset arising from a reacquired right.

Other findings

In acquisitions involving a non-controlling interest in the acquiree, the companies reviewed prefer to recognise the goodwill according to the partial method. With this method, the goodwill relating to the non-controlling interest is not recognised in the financial statements of the acquirer. In anticipation of the change to the standard on the disclosure of interests in other

companies, in its thematic review of the 2011 financial statements the AFM will establish a baseline measurement of the way in which companies disclose non-controlling interests.

A quarter of the companies were involved in a business combination in which they previously had held a non-controlling equity interest. Around half of the companies reviewed provide all the mandatory disclosures regarding the increase of the existing equity interest. The provision of information to users can therefore be improved in this respect.

Two-thirds of the companies disclose the amount of the acquisition-related costs they expensed in the financial year. Capitalisation of the acquisition-related costs as part of the consideration transferred is no longer permitted. The effect of the change in the standard on the result before tax varies. While in some cases this effect is minor, in almost as many cases it is significant. Given the effect that these costs can have on the result for the financial year, the AFM takes the view that there is room for improvement in the financial reporting.

All companies present cash flows from business combinations as cash flow from investment activities. A large majority visibly deduct acquired cash from the cash flow relating to the consideration transferred. This represents a small improvement in comparison to the findings of the AFM's thematic review of the cash flow statements in the financial statements for 2006.

A third of the companies report contingent considerations (or movements thereto) in connection with acquisitions for 2010. The movement schedule of goodwill discloses that a majority of the companies concerned adjusted the cost price of the business combination, as was requested in the previous version of the standard. A small group include an explicit disclosure of the treatment of these contingent considerations or movements.

2 Introduction

By conducting a generic review of certain aspects of financial reporting, the AFM's intention is to raise awareness of important issues.
In this context, the AFM has conducted a review of the application of the standards for business combinations in the financial reporting for 2010.

IFRS 3 discloses how companies should recognise business combinations. This standard was amended in 2008. Companies must apply the changes prospectively to business combinations for which the acquisition date is on or after the beginning of the first reporting period commencing on or after 1 July 2009. Early application is permitted if the changes to the consolidation standard (IAS 27) are adopted at the same time.

When the changes were introduced, the International Accounting Standards Board (IASB) stated that both preparers and users of financial statements will benefit from common, understandable and enforceable principles for the recognition of business combinations. The standard is intended to improve the relevance, reliability and comparability of the information provided by a company regarding a business combination and the effects thereof. To achieve this objective, the standard establishes principles and requirements for how the acquirer:

a) should recognise and measure the acquired identifiable assets, the assumed liabilities and any non-controlling interests in the acquiree in its financial statements;
b) should recognise and measure the goodwill acquired in the business combination or a gain arising from a bargain purchase; and
c) determines what information it must include in its disclosures to enable users of its financial statements to assess the nature and financial consequences of the business combination.

The accounting for the business combination is changed from the purchase method to the acquisition method. The four items to be disclosed by the acquirer in the acquisition method are as follows:

- the identity of the acquirer;
- the acquisition date;
- the fair value of the acquired assets and the assumed liabilities; and
- the goodwill or badwill.

The other important changes can be summarised as follows:

- For each acquisition, the company has the option of either the full goodwill method or the partial method for measuring goodwill and thereby the non-controlling interest.
- Contingent considerations involved in acquisitions must be estimated as accurately as possible at the time of acquisition and recognised in the balance sheet at fair value, even when the probability of payment is considered not to be 'more likely than not'. Changes to contingent considerations at a later date are recognised in profit or loss. Contingent considerations classified as equity may not be remeasured.

- Acquired identifiable assets and assumed liabilities must be measured at fair value on the acquisition date. Indemnification assets, reacquired rights, payments in the form of share-based payments, non-current assets held for sale, contingent liabilities, employee benefits and income taxes form an exception to this general rule.
- Acquisition-related costs are expensed in the period in which they are incurred and the services are received.
- The recognition of step acquisitions is further elaborated.
- The disclosure requirements are extended.

The expectation that many companies would apply the changes to the standard for the first time in their financial statements for 2010, and the topicality of the issue, were reason for the AFM to include this issue in its review.

3 Objectives of the thematic review, design and population

The thematic review of Business Combinations is intended to encourage companies to improve the quality of their financial reporting of business combinations. In addition, the AFM's supervision will contribute to public understanding of the companies concerned and thereby improve the operation of the capital markets. The responsibility for the quality of the financial reporting of course rests primarily with the companies themselves. Compliance with the reporting requirements contributes to confidence in the management of companies.

In this review, the AFM has mapped the information that companies have provided regarding business combinations. The following information in the 2010 financial statements was therefore assessed:

- the information in the statement of accounting principles regarding the recognition of business combinations;
- the disclosure of business combinations that occur during the financial year;
- the disclosure of business combinations that occur in the period between the end of the financial year and the date of preparation of the financial statements; and
- the recognition of business combinations in the cash flow statement.

In addition, the AFM has evaluated the extent to which companies complied with the more extensive disclosure requirements in their 2010 financial statements.

With its previous thematic review of the 2006 financial statements, the AFM investigated the application of the standards for the cash flow statement (IAS 7). The AFM has made a comparison to determine whether the presentation of the cash flows associated with the acquisition of business combinations has improved.

The AFM has to conduct its investigations on the basis of public information. Accordingly, the AFM is not in a position to make an assessment with respect to the following matters:

- The fair value of the acquired assets and the assumed liabilities. Companies are not obliged to disclose the way in which they identify acquired assets and assumed liabilities, or how they determine the fair value;
- The existence of deferred tax assets and liabilities. Companies must measure acquired assets and assumed liabilities at fair value on the acquisition date. The value of these assets and liabilities for tax purposes usually remains unaffected. As a result of this, in accordance with the requirements of IAS 12 Income Taxes, a deferred tax asset or liability is created. Companies are not obliged to disclose the carrying amount of the acquired assets and assumed liabilities immediately prior to the acquisition. It is therefore not possible for the AFM to check whether the measurement at fair value should lead to a deferred tax asset or liability;
- Identification of transactions with the acquiree that are separate from the acquisition of assets and the assumption of liabilities in the business combination. By changing the standard, the IASB has clarified that companies should report these transactions separately from the business combination.

The AFM will put questions to companies when it has doubts as a result of this thematic review regarding whether the company in question has applied the reporting requirements for business combinations correctly. In addition, it will use the results of this thematic review in its risk analysis for the selection of the 2011 corporate financial reporting to be included in next year's review.

The thematic review of Business Combinations is conducted on the 2010 financial reporting of public companies incorporated under Dutch law whose shares are listed on a regulated market in the European Union. The review includes only the financial reporting of companies who entered into one or more business combinations in 2010 (or in 2011 but prior to the preparation of the financial reporting for 2010) that were either individually or collectively materially significant. Approximately 18 percent of these companies made one or more acquisitions in the 2010 financial year. The table shows the type of business combination for companies in each of the indices.

Table 1: Business combinations in 2010 and/or 2011 in the 2010 financial reporting

	Individually material	Collectively material	Both types	Total
AEX	7	2	1	10
AMX	6	2	2	10
AScX	6	1	-	7
Local Netherlands	9	-	-	9
Other EU countries	4	-	1	5
Total	32	5	4	41

Eight companies entered into business combinations in both 2010 and 2011 that were individually or collectively material. The thematic review of Business Combinations relates to 41 companies.

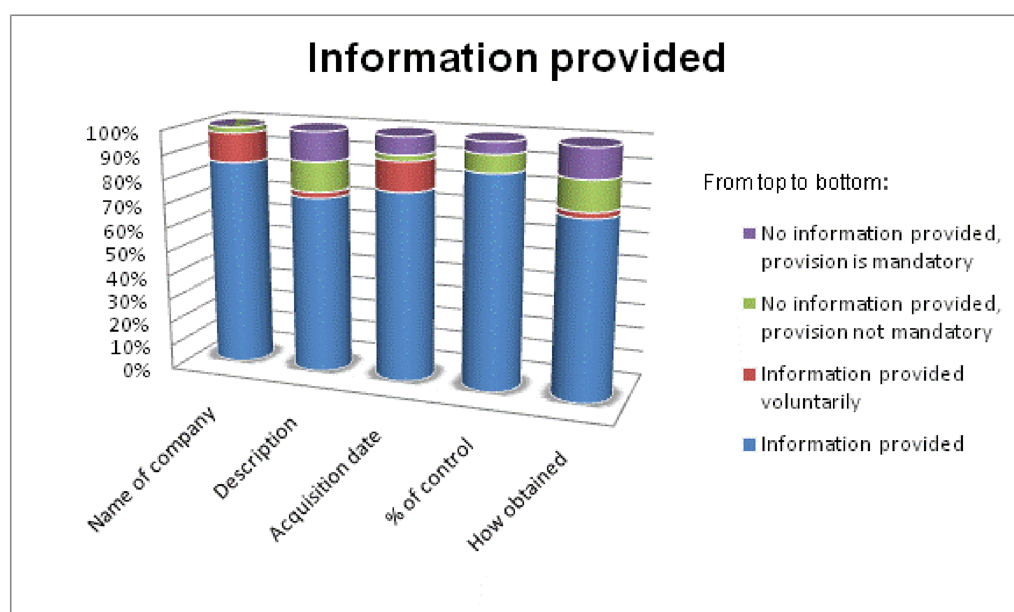
Two of the 41 companies reviewed reported and disclosed business combinations in their financial statements for 2009 in accordance with IFRS 3R.

4 Findings

4.1 Large majority of companies include the mandatory disclosures

A large majority of the companies reviewed include the mandatory disclosures in their financial statements. The acquirer must provide information that enables users of the financial statements to assess the nature and financial consequences of a business combination. To achieve this objective, the standard contains disclosure requirements. The figure shows how the companies reviewed complied with some of these requirements. The findings with regard to compliance with other important disclosure requirements are described below.

Figure 1: Information provided on business combinations



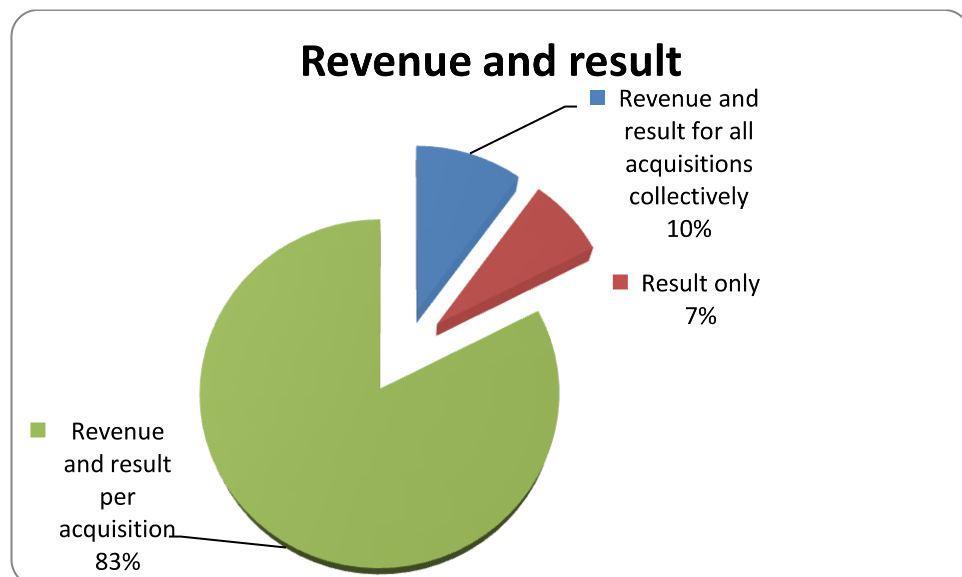
In the case of business combinations that are only of material significance collectively, companies may report totals. The disclosures shown in the figure may in this case be omitted. If this information is nonetheless included in the financial statements, the AFM assumes that this has been done on a voluntary basis. The figure shows that most companies voluntarily report the name of the acquiree and the date of the acquisition. It appears that companies consider this information important for users of the financial statements.

The figure shows that more or less all companies disclose the name of the acquiree, even when this is not required. A large majority disclose, either voluntarily or not, the acquisition date and the percentage of control obtained in the acquiree. Furthermore, more than three-quarters include a description of the acquiree and the way in which control has been obtained. The AFM's conclusion is that a large majority of companies comply with these disclosure requirements.

4.2 Large majority of companies disclose the revenue and result since the acquisition date

A large majority of the companies disclose the revenue and result since the acquisition date as recognised in the consolidated income statement for each materially significant business combination or for business combinations that collectively are of material significance. The disclosure of the revenue is a new disclosure requirement. It is encouraging to note that a large majority of the companies reviewed complied with this new disclosure requirement, especially since in consultation sessions with the IASB and the FASB with respect to the introduction of the amendment to the standard, users of the financial statements indicated that they considered a distinction between autonomous growth and purchased growth to be useful information. The disclosure of the growth that is purchased and the associated revenue assists the users in making this distinction.

Figure 2: Statement of revenue and result per materially significant business combination since the acquisition date



4.3 The consideration transferred is clearly disclosed in a large majority of cases

A large majority of the companies clearly disclose the fair value on the acquisition date of the total consideration transferred for each materially significant business combination or group of collectively significant business combinations. The companies disclose either the total consideration transferred or give a clear disclosure of the various elements of the consideration transferred. In the latter case, the total consideration transferred can be calculated by adding the various components together. Approximately one-eighth of the companies failed to disclose one or more elements of the consideration transferred.

Nearly half of the companies disclose that all or part of the consideration transferred is due at a later date. Approximately half of this group disclose that the liability is contingent in nature. In most cases, this concerns considerations that depend on whether previously established earnings targets are achieved or not. For a very small group, it is clear that the liability concerns a fixed amount. The AFM has to conduct its investigations on the basis of public information. It cannot therefore assess whether the liabilities at other companies are contingent or not. None of the companies concerned included all the mandatory disclosures regarding contingent considerations.

Companies should recognise changes in the fair value of contingent considerations that are designated as a liability in profit or loss in the financial year in which the change occurs. In view of the effect that a change in a contingent consideration can have on the result, the AFM takes the view that companies should devote more attention to these disclosure requirements in their future financial statements.

4.4 A good majority of companies disclose acquired assets and assumed liabilities

At the date of the acquisition, companies must recognise and measure the acquired identifiable assets, the assumed liabilities and any non-controlling interests in the business combination. The difference between the consideration transferred and the amounts allocated represents the realised goodwill or badwill. Three-quarters of the companies disclose the amounts recognised on the acquisition date for each category of acquired assets and assumed liabilities. With regard to individual items, the picture is more complex. These findings are presented in more detail below. In view of their importance and special character, the findings with respect to intangible non-current assets are presented separately in section 4.5.

Acquired assets and assumed liabilities

Three-quarters of the companies disclose the amounts recognised on the acquisition date for each category of acquired assets and assumed liabilities for each materially significant business combination and/or group of business combinations that are of collective material significance. In the remaining financial statements, the AFM found the following:

- only a split between non-current and current;
- only a division of the liabilities into current and non-current; and/or
- companies that collectively disclose multiple business combinations that are actually only *individually* materially significant.

This is not correct. The standard explicitly requires a division into categories of acquired assets and assumed liabilities for each individually materially significant business combination.

The disclosure of business combinations that occur during the financial year

A quarter of the companies state that the initial administration processing of one or more business combinations had not been completed at the time of preparation of the 2010 financial statements. The measurement period may not last longer than one year from the acquisition date. The AFM infers from this that only a limited number of companies will report a possible

change of the allocation of the consideration transferred for business combinations entered into in 2010 in their financial statements for 2011.

The disclosure of business combinations that occur in the period between the end of the financial year and the date of preparation of the financial statements

Different proportions apply for business combinations entered into after the year end but prior to the preparation of the financial statements. None of the disclosures in the financial statements of these business combinations contained all the required information. The AFM infers from this that the accounting for these business combinations is not yet complete. Three-quarters of the companies concerned disclosed the information that could not be provided and the reasons why this was not possible. The most frequently cited reason is the short period of time between the acquisition date and the date of preparation of the financial statements.

Goodwill or badwill

Three-quarters of the companies disclose the amount of goodwill or badwill they recognise for each material business combination or for each group of business combinations that collectively are material. A group of companies of similar size but not similar composition give a qualitative description of the factors that make up the recognised goodwill. A majority of the companies cited synergy and experience of the workforce as important factors. Other factors mentioned included expected growth, access to new geographical markets and expansion of the market position.

Account receivables acquired

A good majority of the companies disclose the fair value of the acquired receivables on the acquisition date. A third of this group additionally report the gross contractual receivable and a best estimate of the contractual cash flow that is expected not to be received. The IASB included these disclosure requirements in the final version in response to comments on the draft version of the amendments to the standard for business combinations. Also from this point of view, the AFM's view is that companies need to improve their compliance with these disclosure requirements in their future financial statements.

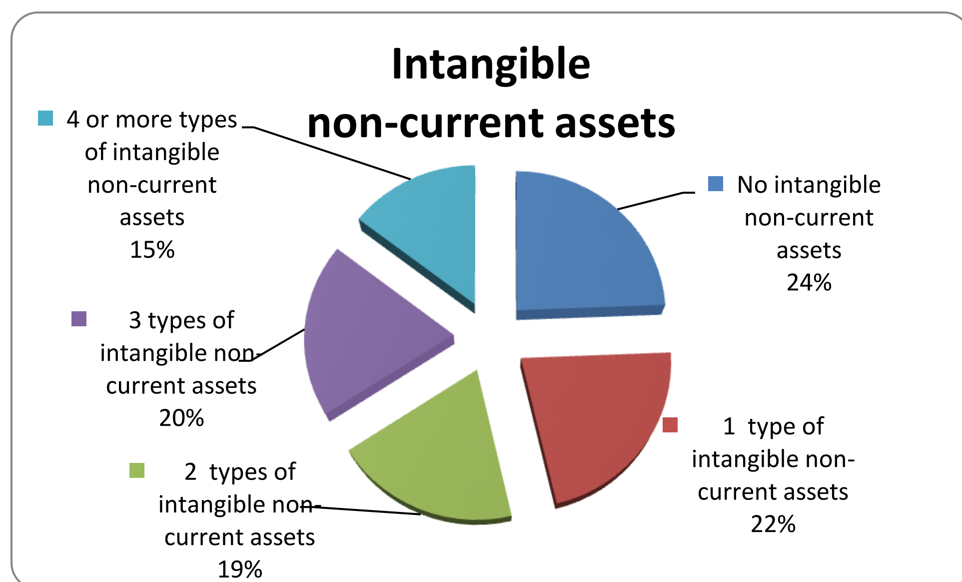
Assumed contingent liabilities

It is notable that only a very small group of companies provide information on the assumed contingent liabilities. None of the companies reviewed state that contingent liabilities are not recognised because they could not reliably establish the fair value. Companies that present this information disclose contingent considerations still payable by the acquiree as a result of previous acquisitions and provisions for guarantees, claims, legal proceedings and tax disputes. Since the AFM has to conduct its investigation on the basis of public information, it cannot assess whether the absence of disclosure of the assumed contingent liabilities is correct.

4.5 A majority of the companies identify intangible non-current assets

Three-quarters of the companies identify and measure one or more intangible non-current assets in their recognition of business combinations. Approximately half of all the companies reviewed disclose the principal reason for entering into the business combination. In virtually all cases, the identified types of intangible non-current assets are consistent with the principal reason for entering into the business combination. Only in one case would the AFM expect there to be additional types of intangible non-current assets on the basis of the principal reason given.

Figure 3: Number of types of intangible non-current assets per company



From the acquisition date onwards, the acquirer must recognise the acquired identifiable assets, the assumed liabilities and any non-controlling interest in the acquiree separately from the goodwill. This can mean that the acquirer recognises certain assets that the acquiree had not previously recognised as assets in its financial statements. For instance, the acquirer will recognise acquired identifiable intangible non-current assets that the acquiree had not recognised as assets in its financial statements because it developed these assets internally and expensed the related costs in its income statement. The standard cites brand names, patents and client relationships as examples of intangible non-current assets.

The most important intangible non-current assets identified are client bases and relationships, brand names, brand rights (or related variables) and software. The specifically designated category 'other' comprises a variety of types of intangible non-current assets, such as technology, databases, development costs and non-competition clauses. A small group of companies identify and measure intangible non-current assets, but do not clearly disclose what type of intangible non-current asset they have recognised.

Table 2: Number of companies with identified types of intangible non-current assets per index

	AEX	AMX	AScX	Local	Other EU	Total
Clients	5	6	3	5	-	19
Brands	5	3	4	2	1	15
Software	4	2	2	1	1	10
Order book	-	2	1	2	-	5
Patents	1	-	2	-	-	3
Publishing rights	2	-	-	1	-	3
Other	3	1	4	2	3	13
Unknown	1	4	1	1	-	7

Reacquired rights constitute a special category of intangible non-current assets. The standard gives guidelines for the recognition and accounting of reacquired rights. Reacquired rights are rights that the acquirer had granted to the acquiree and are reacquiring as a result of the business combination. Examples of such rights are the use of a trading name in the context of a franchise agreement, or a right to use the technology of the acquirer. The standard states that a reacquired right is an identifiable intangible non-current asset that must be recognised separately from the goodwill. None of the companies reviewed identify an intangible non-current asset arising from a reacquired right.

4.6 In acquisitions involving a non-controlling interest, a large majority of the companies prefer to recognise goodwill using the partial method

Almost half of the companies effected one or more acquisitions in 2010 in which the business combination involved a non-controlling interest (or NCI) at the time of the acquisition. All the companies involved disclosed the recognised amount of the NCI on the acquisition date. Three-quarters of the companies concerned determine the goodwill on the basis of the partial method.

For each business combination, the acquirer must measure the NCI in the acquiree either at fair value or at the proportion of the identified net assets represented by the non-controlling interest (the partial method). If the NCI is measured at fair value, the goodwill on the NCI will also appear in the financial statements of the acquirer. With the partial method, this is not the case. The decision as to which method to apply can be made on the acquisition date and may be made separately in each case. The decision affects the measurement of the NCI in all periods subsequent to the acquisition date, and the test for impairment of goodwill. Companies must recognise subsequent acquisitions of the NCI as a transaction between shareholders. No additional goodwill may be recognised in this case. The difference between the carrying amount of the NCI and the acquisition price must be expensed to the company's reserves.

The decision made on the acquisition date can thus affect the company's balance sheet ratios and solvency in the longer term. The advantages and disadvantages of the two measurement methods may vary depending on the expected development of the business combination. The

AFM therefore expects that companies will select one of the two measurement methods for each business combination.

The following example illustrates the effect of the method used to determine the goodwill.

Table 3: Recognition of an NCI

On 1 January 2010 company A acquires 70% of the shares in company B. The consideration transferred is €700. The fair value of the 30% NCI is estimated at €350. The fair value of the balance of the identifiable acquired assets and the assumed liabilities on the acquisition date is €800. Company A can recognise the goodwill in two ways:

	NCI at fair value (full goodwill)	NCI at proportion of net assets of acquiree (partial goodwill)
NCI	€350	€240 (30% * €800)
Goodwill	€250 (€700 + €350 - €800)	€140 (€700– 70% * €800)

The consolidation project of the IASB included a review of the disclosure requirements with regard to NCIs. These disclosures are intended to enable the users of the financial statements to obtain a better understanding of the effects of NCIs on the financial position, financial results and cash flows. The disclosure requirements in the new standard for disclosure of interests in other entities (IFRS 12) are more extensive than those included in the current consolidation standard (IAS 27). In most cases, one cannot identify the items to which NCIs relate from the financial statements. Investors have indicated that they are interested in the answer to this question, so that they can form an independent opinion regarding the effects of NCIs on the various ratios. The AFM intends to carry out a baseline measurement of how companies disclose NCIs by means of a thematic review of the 2011 financial statements.

4.7 A quarter of the companies reviewed achieved a business combination in stages in 2010

A quarter of the companies entered into one or more business combinations in 2010 whereby they already held an NCI prior to the acquisition date. Three-quarters of these companies disclose the fair value of this interest at the time of the acquisition. A small minority of these companies report the amount of the result arising from the adjustment of the carrying amount of the NCI to fair value. Approximately half of these companies disclose the item in profit or loss to which this result is expensed.

In a business combination that is achieved in stages (a ‘step acquisition’), the acquirer must adjust the carrying amount of its previously held interest to the fair value on the acquisition date. The result of this adjustment must be recognised in profit or loss in the year in which control is obtained. In view of the effect that this adjustment can have on the result for the year in question, the AFM takes the view that companies need to devote additional attention to the observance of these disclosure requirements in future.

4.8 The change to the treatment of costs relating to the acquisition has various effects on the result before tax

A large majority of the companies state the amount of the acquisition-related costs they expensed in the financial year. Capitalisation of the acquisition-related costs as part of the consideration transferred is no longer permitted. The effect of the change in the standard on the result before tax varies. While in some cases this effect is minor, in almost as many cases it is significant.

Acquisition-related costs are costs the acquirer incurs in order to effect a business combination. These costs include professional fees for advisers, lawyers, accountants, valuers, experts and consultants. The acquirer must expense these costs in the period in which the related services are received. Capitalisation of these costs as part of the consideration transferred is no longer permitted.

In order to measure the effect of the changed method of recognition of acquisition-related costs, the AFM has compared the reported costs to the consideration transferred and the result before tax for 2010. The results are shown in the table below. The first column lists the results for the reported costs as a percentage of the result before tax in 2010. The second column shows the results for the reported costs as a percentage of the consideration transferred.

Table 4: Number of companies per percentage group of the acquisition-related costs in comparison to the result before tax in 2010 and the consideration transferred

	Result before tax in 2010	Consideration transferred
0.0% - 0.5%	8	5
> 0.5% - 1.0%	3	7
> 1.0% - 1.5%	2	3
> 1.5% - 2.0%	4	2
> 2.0% - 2.5%	1	3
> 2.5% - 3.0%	4	2
> 3.0% - 5.0%	1	2
> 5.0%	5	4
Acquisition-related costs unknown	13	13
Total number of companies	41	41

4.9 All the companies present cash flows from business combinations as cash flow from investment activities

All companies (100 percent) present in their cash flow statement the cash flow resulting from the acquisition of subsidiaries or other business divisions as separate cash flow within the cash flow from investment activities. In a large majority of cases (85 percent), a comparison between the cash flow from investment activities in question and the disclosure of business combinations reveals that these companies have deducted the cash acquired from the total cash flow arising from the acquisition of subsidiaries or other business divisions. This represents a slight improvement on the results of the AFM's thematic review of the financial statements for 2006, and demonstrates that the reporting of cash flows arising from the acquisition of subsidiaries or other business divisions has improved since the 2006 financial year.

With its previous thematic review of the 2006 financial statements, the AFM investigated the application of the standards for the cash flow statement (IAS 7). The report of this review states that 80 percent of the companies present the cash flow arising from the acquisition of subsidiaries or other business divisions as separate cash flow within the cash flow from investment activities, while 74 percent of the companies deducted the cash acquired from the total cash flow arising from the acquisition of subsidiaries or other business divisions.

The standard for the cash flow statement states that the separate presentation of cash flows arising from investment activities is important, because these cash flows give an indication of the degree to which expenses are incurred for assets that are intended to generate revenue and cash flow in future.

4.10 A good majority of the companies recognise changes to contingent considerations of previous business combinations according to the previous version of the standard

A third of the companies recognise (movements in) contingent considerations in 2010 that relate to business combinations created prior to the 2010 financial year. An eighth of the companies involved explicitly disclose the method whereby (movements in) these contingent considerations are recognised. From the changes in related balance sheet items, it can be seen that in a good majority of cases, movements in contingent considerations are still recognised according to the previous version of the standard. This is mainly visibly in the movement schedule of the goodwill, since under the previous standard the acquisition price of the business combination had to be adjusted to reflect movements in the contingent consideration. In the remaining cases, it is not possible to establish with certainty how these contingent considerations are recognised.

From the above, the AFM infers that a good majority of the companies concerned are prospectively applying the changes in the standards for business combinations in accordance

with the transitional provisions. A more explicit disclosure of the method of recognition of (movements in) materially significant contingent considerations relating to business combinations created prior to the application of changes to the standard would be welcomed by the AFM.

The Netherlands Authority for the Finanacial Markets
T +31 20 797 3721
P.O. Box 11723 | 1001 GS AMSTERDAM

www.afm.nl

Amsterdam, February 2012