

On your marks...

Get set?

Major European retailers position themselves in the early stages of the race to implement IFRS

Entering the first lap

The establishment of the opening IFRS (International Financial Reporting Standards) balance sheet represented a major step in the transition to IFRS by listed European groups. In order to restate their 2004 consolidated accounts (previously prepared in accordance with local GAAP (Generally Accepted Accounting Principles)) under IFRS, it was necessary to adapt and to mobilise additional resources. However, despite the significance of this step, the groups have in fact only left the starting blocks in the race for IFRS implementation. Now begins the real race. The goals: improved financial transparency and comparability. The challenge: keeping up to date with the evolutions due to occur in the standards themselves. It is a race but a long one. The key: endurance and adaptability.

IFRS: a moving target

In addition to the evolutions of the standards per se, an additional factor needs to be taken into account, that of the interpretations of these same standards. The IFRS framework is a generic one. It does not provide guidance on industry-specific matters and hence, needs to be adapted for every sector where it is applied.

The retail sector is a case in point. Retailers do not yet have the necessary hindsight to ensure that the standards have been interpreted in a consistent, comparable way across the industry. Such convergence can only be achieved over time through a series of adjustments to each group's accounting positions, to eventually reach the comparability which the new standards aim to provide.

Accordingly, it is realistic to expect that the rules applied by certain retailers in establishing their opening IFRS balance sheets and restated 2004 financial statements, such as calculating impairment losses (e.g. defining their CGUs) or supplying segment information, will evolve as industry best practice in applying IFRS develops.

The evolutive nature of IFRS is also driven by the fact that the IFRS framework is a principles-based one. This is in direct contrast to the rules-based accounting frameworks that have tended to apply in most European countries in the past. IFRS seeks to adapt itself to the economic realities of transactions to which it is applied. Since October 2002 it has also progressed, and continues to do so, towards a convergence with US GAAP.

And even though the transition to IFRS on 1 January 2005 was achieved from a position of relative stability (the so-called "stable platform"), the fact remains that the IASB already has a number of revisions planned. Some of these will have a major impact on the retail sector, such as the project on Performance Reporting and the planned revision of IAS 14 Segment Reporting, which is due to converge with the US GAAP statement SFAS 131.

More comprehensive disclosure

As mentioned before the establishment of the Opening IFRS Balance Sheets was only the first step, albeit an important one. The question now is, will the groups rise to the challenge imposed by the preparation and presentation of their 2005 financial information, in particular the elaboration of the notes to the financial statements? Successfully achieving this will be directly dependent on the quality and relevance of the changes made to groups' information systems, as well as their willingness to play the game of financial transparency.

Adopting IFRS needs to be seen as a long-distance race, not a sprint. The starting pistol was fired on 1 January 2005. The various companies now have to pace themselves for the duration of the entire race and above all, remain flexible to meet the challenges hidden just around the corner after this initial stage.

In addition, groups will be expected to play a key role in contributing to the ongoing standard-setting process of the IASB by sharing their practical experience. This growing involvement means that the industry-specific interpretation of standards, as set out in the rest of this document, will become increasingly crucial, especially for the retail sector.



Benchmarking the retail sector

In summer 2004, Deloitte carried out a benchmarking study of the retail sector entitled **On your marks! Just how ready is the retail industry for IFRS?** This study was designed to measure the likely impact of the new standards, both at the conceptual level and in terms of practical solutions to implementing the IFRS standards in the retail industry.

The study analysed a representative sample of European retailers, and highlighted areas of convergence as well as the differences in interpretation of IFRS. The study identified and anticipated the key challenges which the industry would face as it transitioned to IFRS.

For every listed retail group, the transition to IFRS involves some degree of transformation. However, the extent of these changes depends on the nature of existing local GAAP and in particular the significance of and complexity resulting from the differences between those standards and IFRS. One of the conclusions of the initial study was that not all retailers had worked with the same level of commitment in preparing for the transition and that, "a significant proportion of retailers still have work to do if they are to meet IFRS deadlines".

The establishment of the opening IFRS balance sheets and restated 2004 group financial statements has been completed, and hence, over the past few months the various groups have been unveiling the implications of IFRS on their businesses to the analysts. As a result, Deloitte decided to perform a new benchmarking study to highlight the actual impact of the

transition to IFRS on the retail sector, and to judge whether one of the essential goals of IFRS – to enable improved comparability between groups – has in fact already been achieved as part of this transition.

The approach adopted for this study entailed:

- selecting a representative sample of European retailers who had already published information under/concerning their transition to the new standards;
- identifying the major impacts of the transition to IFRS for each of the selected retailers;
- comparing the technical positions and accounting treatments applied in establishing their opening IFRS balance sheets as well as the accounting policies retained under IFRS.

Our study concentrates mainly on those IFRS standards whose application raises specific issues for the retail industry. There are, of course, a number of accounting options or treatments related to the application of other IFRS standards, where the choices to be made or the impact is not sector specific.

The groups selected for inclusion in this study form a representative sample of the major players in the European retail industry.

All our analyses are based on financial information communicated to the market up to 29 June 2005, either by means of formal financial statements and their subsequent updates or the presentations

to analysts on the impact of the transition to IFRS, available on the appropriate groups' websites.

The list of groups as well as the sources of information we have used are as follows:

- AHOLD* (2004 Annual Report).
- CARREFOUR (29 June 2005 Presentation to analysts).
- CASINO (15 April 2005 Presentation to analysts).
- DELHAIZE* (2004 Annual Report, 1 December 2004 Presentation to analysts, 2004 IFRS accounts published 4 May 2005).
- METRO (2004 Annual Report).
- TESCO (25 February 2005 Presentation to analysts).
- PINAULT-PRINTEMPS-REDOUTE (2004 Annual Report, 17 January 2005 Presentation to analysts).
- KINGFISHER (17 March 2005 Press release).

* Groups listed in the USA and producing US GAAP reconciliations.

We would like to clarify that Deloitte is not expressing any opinion on the IFRS restatements identified by the groups included in this study. This non-comprehensive benchmarking only aims to highlight areas of convergence, differences and potential areas for development related to the retail industry's transition to IFRS.



Segment reporting (IAS 14)

One of the most notable results of the transition to IFRS relates to the volume of information to be disclosed in the notes to the consolidated financial statements.

The IFRS requirements regarding this are much more demanding than under previous local GAAPs. In particular, IFRS requires the presentation of strategically aggregated financial information (so called "segments") in a way that is economically appropriate and useful to the users of such financial information.

IAS 14 defines two levels (reporting formats) at which segment information needs to be provided, with an emphasis, and hence more information, on the first of these two levels. The manner in which a group's risks and returns are managed will largely determine the choice of primary versus secondary reporting format. So, for instance, if a retailer believes that its risks and returns are affected principally by the products and/or services that it supplies rather than the geographical areas where it operates, it will choose 'business segments' as its primary reporting format and 'geographical segments' as secondary.

When applied to the retail industry, the geographical segments can be groups of countries (a zone), individual countries, or regions within a country. Similarly, business segments can be activities (grocery or general retail, wholesale, specialist stores...), formats (such as hypermarkets or supermarkets within the same trade) or retail brands (within the same format).

This demonstrates, once again, the potential problem of consistency between the approaches followed by the different groups in choosing their segment reporting formats. It also leads us to ask the question: "Will retailers play the game of financial transparency by segmenting their activities in such a way as to be economically pertinent?"

From this analysis, it is clear that single activity groups such as Carrefour and Casino, have chosen geographical zones as their primary reporting format, with formats (hypermarkets, supermarkets) as the secondary. Multi-activity groups, by contrast, have chosen to use their activities, and hence "business", as primary reporting format, with geographical groupings second.

It is interesting that groups such as Delhaize and Tesco are only providing information for their primary reporting format, geographical zones. In the case of Delhaize, for example, its US activities represent 70 % of its revenue and aggregates several different activities and brands.

As for Ahold, the group has chosen to disclose the same level of detailed information for its secondary reporting format as for its first.

It is thus clear that the way in which segment information is presented and the level of detail provided for each segment differs depending on the retailer. The choice of reporting formats appears to be largely dependent on the actual organisation of the groups' activities (single versus multi). Nevertheless, the consistency of this information will only be a tangible reality in the years to come. The segment information as currently defined and disclosed by the groups is thus likely to evolve as industry best practice develops.

The companies in our sample have provided the following segmental analyses:

	Carrefour		Casino		Metro		Ahold		Delhaize		Tesco	
	Level 1	Level 2	Level 1	Level 2	Level 1	Level 2	Level 1	Level 2	Level 1	Level 2	Level 1	Level 2
	geographic business		geographic business		business		geographic business		geographic		N/A	
Revenue	•	•	•	•	•	•	•	•	•	N/A	•	N/A
Cost of sales									•	N/A		N/A
Gross margin									•	N/A		N/A
Operational expenses									•	N/A		N/A
EBIT/EBITDA/ Operating profit	•		•		•	•	•	•	•	N/A	•	N/A
Depreciation	•				•	•	•	•	•	N/A		N/A
Segment assets	•		•		•	•	•	•	•	N/A	•	N/A
Segment liabilities	•		•		•	•	•	•	•	N/A		N/A
Investments	•	•	•	•	•	•	•	•	•	N/A		N/A
Impairment									•	N/A		N/A

Note: PPR and Kingfisher had not at June 2005 published any information regarding their choice of primary versus secondary reporting format under IFRS.

Revenue (IAS 18)

IAS 18 is relatively equivocal concerning the rules and methods to be applied for revenue recognition. It defines revenue as the gross inflow of economic benefits during a period arising in the course of the ordinary activities of an entity. Such revenue must be measured at the fair value of the consideration received or receivable which is nothing other than the amount of cash or cash equivalents received or receivable by the entity.

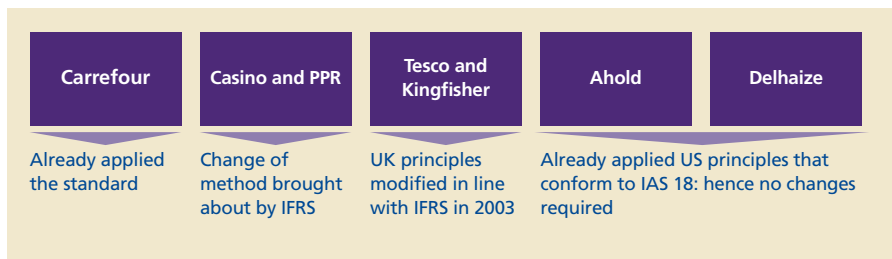
Accordingly, it is clear that the IFRS standards follow a highly generic approach.

However, revenue recognition requires a much more sector-specific approach. In effect, the methods for revenue recognition (when to account and at what value) are heavily dependent on the structure of the retailers' sales activities, their commercial agreements with customers (e.g. how customer loyalty programmes are treated) and suppliers (e.g. rate/tariff agreements).

Following the US accounting framework for practical application guidance

The generic rules set out under IAS 18 are not sufficiently detailed or specific to answer the questions surrounding the accounting for revenue. As a result, the principles applied in recognising revenue under IFRS will draw, to a great extent, on the guidance developed by another accounting framework, similar in nature and spirit for purposes of the recognition of revenue to IFRS, namely US GAAP.

In this respect, applying these rules to the retail sector may well involve major changes in the accounting for revenue. For instance, the commercial terms that retailers negotiate with their suppliers (in the form of rate/tariff agreements or other agreements) are generally regarded as forming part of purchase costs, i.e. they should not be recognised as income but rather as reductions in cost of sales. And it goes even further: by including these commercial advantages in purchase costs, the value of individual inventory items will also need to be adjusted.



This means that all commercial initiatives, whether they be one-off or recurring in nature, that aim to boost sales and increase customer loyalty, concluded in conjunction with suppliers or by the retailers alone, impact the accounting for revenue, purchases and provisions, and must be analysed on a case-by-case basis.

From our analysis of the chosen sample of retailers, it became clear that only two of the eight groups (Casino and Pinault-Printemps-Redoute) had changed their accounting policy for revenue recognition as a result of the transition to IFRS. In Casino's case, this involved reclassifying sales revenues either to other income or as a reduction in cost of sales, to the value of €1,984 million. PPR identified a major disparity in the way that its Printemps concession contracts were accounted for, with sales revenues being treated differently depending on whether the group was considered to have acted as the principal or as an agent in IFRS terms. In the latter case, only the commission received is to be recorded as revenue.

The group also changed its policy for the recognition of revenue from the sale of goods linked to extended guarantees, the income from these transactions being recognised over the period of the guarantee under IFRS.

The lack of impact on revenue recognition upon transition to IFRS for the other retailers we studied is essentially due to the fact that some of them were already applying policies in line with IFRS rules under previous local GAAP. This was the case of Carrefour of which the policies used to produce its group accounts under previous local GAAP were already very close to those recommended under IFRS. As a result, there were no major discrepancies in revenue recognition. The same is largely true of Tesco and Kingfisher (formerly reported under UK GAAP) and Ahold and Delhaize (formerly reported under US GAAP).

The transition to IFRS thus resulted in a convergence of the revenue recognition methods used by the various retailers.



Inventories (IAS 2)

IAS 2 sets out the rules for determining the cost of inventories. This must include all the costs of purchase, costs of conversion and other costs incurred in bringing the inventories to their present location and condition.

As explained under **Revenue (IAS 18)** above, commercial initiatives entered into with suppliers must henceforth be considered as improvements to purchasing conditions, which will result in a reduction in the value of inventories for those retailers who until now have treated such advantages as revenue or a reduction in marketing expenses.

The impact of IAS 2 on the cost of inventories will hence have as effect, on one hand, an increase in delivery costs to the points of sale and on the other, a decrease in the cost price of the products resulting from the reclassification of commercial advantages as described above.

Our analysis of the sample of retailers selected reveals that the issues associated with the practical application of the rules for inventories as set out in IAS 2 has mainly impacted French groups. Both Carrefour and Casino have had to change the way they account for inventory costs, with one having to include delivery to point-of-sale costs, supplier discounts and services billed to customers, while the other only delivery to point-of-sale costs. The transition to IFRS thus appears to reveal a certain consistency in accounting for inventory costs among retailers, with the exception of the French groups. This is as a result of the fact that previous local GAAPs had a less extensive scope for including costs in the cost of inventories. This discrepancy has, however been addressed by the transition to IFRS.

Even though the convergence of policies applied in determining the costs of inventories by the various groups seems clear cut, it is nevertheless difficult to judge whether the accounting treatments applied to the gross value of inventories and the related write-downs (application of the NRV (net realisable value) method) are perfectly consistent.

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	Carrefour	Casino	Métro	Ahold	Tesco	Groupe Delhaize	Kingfisher	PPR
Chosen definition for delivery costs	All logistics costs up to the point where goods are placed into store stock rooms	Warehousing and downstream transportation costs between the warehouse and the store	No detailed information provided in published financial accounts	Inventory costs include all the costs incurred in bringing the inventories to their present location and condition	No detailed information provided in published financial accounts	No detailed information provided in published financial accounts	Inventory costs include all the costs incurred in bringing the inventories to their present location and condition	For Printemps and Gucci measurement at sales price after corresponding reduction in margin and mark-downs

Impairment of Assets (IAS 36)

All retailers can or do have under-performing assets. How these are identified and the performance of the related impairment tests are set out in IAS 36 and involve:

- carrying out impairment tests (e.g. goodwill as well as intangible assets with indefinite useful lives, must be tested on an annual basis at the same date every year. Appropriate indicators of impairment (so called “trigger events”) must also be defined in order to carry out impairment tests for tangible and intangible assets with finite useful lives);
- defining CGUs (Cash-Generating Units – the smallest identifiable group of assets that generates cash inflows that are largely independent of the cash inflows from other assets or groups of assets);
- allocating goodwill to the CGUs that are expected to benefit from the synergies of the business combination that gave rise to such goodwill;
- calculating recoverable amount and in particular, value in use (the nature, the origin of cash flows and their future prospects, discount rate).

This process is nevertheless open to differing understandings and hence interpretations by individual retailers. This raises various questions including whether assets are tested at the same level across the whole industry, and whether the same “trigger events” have been defined for different retailers?

Looking at our sample of retailers, it is still difficult to give precise answers to all of these questions. The convergence and harmonisation of the principles applied will no doubt occur in the years to come if the various retailers continue to work with this goal in mind.

More generally, the practical implementation of IAS 36 has not had any major impact on the retailers included in our study (apart from Delhaize). Most believe that the rules and regulations applied under previous local GAAP were not far removed in spirit from IAS 36.

Defining CGUs

When it comes to defining CGUs, our sample of retailers chose the following levels at which to test their assets (see table overleaf):

The sample tested did not reveal any great consistency as to the level at which traditional assets (see definition in the table overleaf) are tested. However, the general trend appears to be to recognise individual stores as CGUs for impairment testing purposes. Indeed, amongst the companies that have published this information, only Metro and PPR test their assets for impairment at a higher level (that of brand by country).

Allocating goodwill to CGUs

It is interesting to note that information about the level at which goodwill is tested is not always disclosed.

More than half the population included in the sample did not provide any information as to how goodwill is allocated to CGUs and at what level it would be tested.

According to IAS 36, goodwill must be allocated to CGUs or groups of CGUs that are expected to benefit from the synergies of the business combination/s that gave rise to the goodwill and such allocation must be disclosed in the notes to the financial statements.

Moreover, the level at which goodwill is tested must represent the lowest level at which goodwill is monitored for internal management purposes. In addition, this cannot be at a level superior to those defined for segment reporting purposes.

However the level at which goodwill is tested has a direct and significant impact on the impairment or otherwise of the CGUs. The higher the level at which the goodwill is tested, the less likely the retailer will be to record an impairment loss. For instance, if goodwill is tested at a geographical zone level covering several individual CGUs (stores), the margins of those stores in the region that are performing well will compensate for the under-performance of other stores in the same region, and will thus neutralise the impact of these under-performing CGUs on the value of the goodwill. In this case, there would be no impairment of goodwill to take into account.

It could be a completely different situation if goodwill is no longer tested at geographical zone level, but at individual store level. The value of the goodwill would be directly affected by the performance of the CGU/store to which it is allocated. This would result in an irreversible impairment loss being recorded against goodwill for the under-performing stores.

This raises the question, for such stores, whether the financial problems they are encountering are due to lasting and fundamental structural difficulties or whether they are simply the result of short-term economic trading issues.

Company	Nature of assets	CGUs defined			
		Stores	Brands by country	Operating units	Networks
Carrefour	Traditional assets Goodwill		No published information No published information		
Casino	Traditional assets <i>Hyper and supermarkets</i> <i>Other networks</i> Goodwill	•			•
Méto	Traditional assets Goodwill		• •		
Ahold	Traditional assets Goodwill	•			
Tesco	Traditional assets Goodwill		No published information No published information		
Delhaize Group	Traditional assets Goodwill	•			•
Kingfisher	Traditional assets Goodwill		No published information No published information		
PPR	Traditional assets Goodwill		• •		

Traditional assets = Intangible and tangible assets excluding goodwill

So, depending on the level at which CGUs are identified, the accounts will reflect the effects of fluctuations in the performance of individual stores on a more or less real-time basis.

It is important to keep in mind that it is essential to correctly define the level at which goodwill will be tested, in order to be able to deal with the complexities related to the determination of the recoverable amount of the assets concerned.

Other points of interest

The retailers in our sample have yet to publish specific information regarding a number of issues:

- Although goodwill and intangible assets with indefinite useful lives must be tested annually in a systematic way on a defined date, none of the retailers in our study disclosed the date chosen to carry out these tests (e.g., a date close to the cut-off point for half or full-year reporting).
- None of the retailers covered by this study disclosed whether they have established the impairment indicators which would trigger the performance of impairment tests. In the retail sector, for example, it is possible to imagine a threshold being set for the variation between the budgeted and actual turnover achieved by a particular store, to act as an indicator for an impairment test to be performed.

As our study underlines, the transition to IFRS is only the first stage in the move towards achieving a consistent impairment model for the retail sector.

Elaborating the notes the IFRS financial statements

If the momentum generated by the application of IAS 36 in establishing groups' opening IFRS balance sheets and restated 2004 financial statements is well established, retailers will remain under significant pressure to provide more in-depth financial information. The issue of preparing the additional notes to the 2005 financial statements as required under IFRS still has to be addressed. In this respect, significant information about asset impairments will need to be disclosed, and this will involve major structural decisions and a resulting modification or installation of new reporting tools. For example, companies will have to provide an explanation for all the estimates used to determine the recoverable amount of CGUs containing goodwill or intangible assets with indefinite useful lives.



Property, Plant and Equipment (IAS 16)

IAS 16 sets out all the accounting and measurement rules for tangible fixed assets.

Such assets are initially accounted for at their cost of acquisition and are subsequently measured either at their revalued fair value (changes in fair value being recorded directly in a separate component of equity) or depreciated cost. They must be depreciated over their useful lives, using a depreciation method that reflects the pattern in which the assets' future economic benefits are expected to be consumed by the entity.

Depreciated cost or revaluation method?

The subsequent measurement of tangible fixed assets raises the question of how consistent the choice of valuation method among the various companies in the retail sector is (i.e. depreciated cost versus revalued amount)? In addition, the difficulty of estimating useful lives and potential residual values for purposes of calculating depreciation needs to be considered.

The first question to be asked is thus: which method have retail groups adopted for the subsequent measurement (after initial recognition) of their tangible fixed assets? Fact is, the choice appears to be consistent: depreciated cost. The transition to IFRS did thus not generate any additional inconsistencies in treatment among the various groups.

Will the transition to IFRS result in a change in the estimation of useful lives?

Our earlier study of retailers' readiness for IFRS – **On your marks! Just how ready is the retail industry for IFRS?** (issued in July 2004) – revealed that assessing the useful life of a tangible fixed asset and so, indirectly, its residual value, presented a major concern for the retailers we interviewed. As a result, it is interesting to see how IAS 16 has been applied in practice in this regard. Has the transition to IFRS led to a new approach in assessing the useful lives of assets?

Amongst our sample group of retailers, only the French groups, Carrefour and Casino, had modified their estimations of the useful lives of certain tangible fixed assets (effectively prolonging them), namely buildings.

These two groups explained that this re-estimation resulted in a more relevant presentation of the expected economic useful lives of their buildings, the period having been increased from 20 years under previous local GAAP (French) to 40 years under IFRS.

Apart from PPR, the other French retailers in our sample group all had shorter depreciation periods for property (20 years) than their European counterparts. The transition to IFRS would thus appear to allow for greater consistency in estimating the useful lives of tangible fixed assets in the retail sector by giving French groups the opportunity to increase their previous estimations in this regard.

Does the determination of residual value pose a problem for the retail industry?

Analysing the impact of the transition to IFRS on the determination of the residual values of tangible fixed assets at the end of their useful lives is less straightforward.

Only the French groups, Carrefour and Casino, treated this issue, notably by setting all residual values to zero. None of the other European retailers in our sample group provided detailed information in this respect.

However, if the question of how to assess residual value does arise, retailers appear to be willing to regard the residual values of their tangible fixed assets as equal to zero or not material, while arguing (as Carrefour does in its 2004 Annual Report) that: "as retailers are not in the business of selling their assets, the residual value of a building at the end of its depreciation period will be zero and so tangible fixed assets will always be fully depreciated".

Useful life of buildings	Carrefour	Casino	Metro	Ahold	Tesco	Groupe Delhaize	Groupe PPR	Kingfisher
Transition to IFRS	Possible impact	Definite impact	N/A	No impact	No impact	No impact	No impact	No impact
Depreciation period used under previous local GAAP	20 years	20 years	between 10 and 33 years	<ul style="list-style-type: none"> stores: 30 to 40 years other buildings: 25 to 30 years 	No detailed information given	40 years	20 to 40 years	20 to 50 years
New depreciation period under IFRS	40 years	40 years	No change	No change	No change	No change	No change	No change

Identifying and assessing investment property

The transition to IFRS also raises another issue surrounding tangible fixed assets, that of identifying and assessing so-called investment property.

IAS 40 defines investment property as, "land and/or buildings held to earn rentals or for capital appreciation or both". Such assets must be measured at fair value (changes in fair value being recorded in the income statement) or depreciated cost.

Whichever measurement method a particular retailer chooses, the fair value will still have to be calculated. Even if the depreciated cost method is used, fair value still has to be specified in the notes to the financial statements.

One issue which often comes up in the retail sector relates to the treatment of shopping centres or malls. How have retailers opted to account for these types of properties upon transition to IFRS?

An analysis of the positions taken by the retailers in our sample shows that there is still a degree of divergence within the sector. Of the eight groups analysed, only Carrefour and Tesco actually tackled this issue in their presentations about the impact of IFRS on their businesses. They both consider shopping malls as being investment properties. However, the measurement methods chosen by the two groups differ.

Carrefour has chosen to measure its shopping malls using the depreciated cost method, and so it did not identify any financial impact linked to the treatment of investment property in its opening IFRS balance sheet at 1 January 2004.

Tesco, on the other hand, reclassified in its consolidated accounts for 2004/2005 £539 million of buildings (previously classified in Property, Plant and Equipment) as investment property, without any resulting impact on the income statement.



Goodwill and Intangible Assets (IAS 38 and IFRS 3)

IFRS 3 indicates that business combinations should be accounted for using the purchase method. This involves the buyer (acquirer) recognising the identifiable assets, liabilities and contingent liabilities of the acquiree at their fair value at the date of acquisition. Any portion of the cost of the business combination (the purchase price) not allocated to the abovementioned elements is accounted for as goodwill. This goodwill is no longer amortised, in contrast to previous local GAAPs.

Upon transition to IFRS, companies may use the exemption provided under IFRS 1 **First-time adoption of IFRS** that releases groups from the obligation to restate, retrospectively, all business combinations under IFRS 3 **Business Combinations**.

All retailers in our study, with the exception of PPR, chose not to restate their business combinations that had taken place prior to 1 January 2004. The impact of the transition to IFRS was thus limited to the discontinuance of goodwill amortisation.

PPR, however, did restate its prior business combinations. IFRS 1 allows groups to choose a date (prior to 1 January 2004) from which they will restate: in the case of PPR, this was 1 January 1999 – corresponding to the date of acquisition of Gucci. This restatement resulted in an increase in the value of the brand of more than €1,4 billion, an increase in goodwill of over €1 billion, an increase in minority interests of more than €1,2 billion and the recognition of a deferred tax liability related to the brand of €1,2 billion.

The impact of transition on recognising intangible assets

In accounting for their pre-transition business combinations, groups had the opportunity to identify and recognise certain intangible assets.

Not performing a full retrospective restatement of business combinations prior to transition, i.e. using the exemption provided in IFRS 1 as explained above, does not excuse groups from reassessing the relevance of intangible assets previously recognised as part of such business combinations.

IAS 38 Intangible Assets defines an intangible asset as an identifiable non-monetary asset, without physical substance, controlled by the entity. This definition is more restrictive than those included in previous local GAAPs.

Accordingly, the transition to IFRS could give rise to reclassifications of intangible assets recognised under previous local GAAP to goodwill, e.g. market share – this does not meet the recognition criteria under IFRS. Of the groups included in our study it was, once again, only the French groups that were affected by this change. Casino reclassified prime locations and market share previously accounted for as separate intangible assets to goodwill, resulting in a negative impact on equity of €245 million at 1 January 2004. Similarly, PPR reclassified market share and goodwill calculated under previous local GAAP to goodwill under IFRS.

The application of IAS 38 is starting to promote a degree of consistency in the way companies recognise intangible assets.

Accounting for goodwill on acquisitions of foreign entities

The transition to IFRS could also have an impact on the accounting for goodwill arising upon the purchase of a foreign entity. In effect, IFRS requires that such goodwill should be recorded in the functional currency of the foreign entity purchased. And, as a result, the goodwill will be converted to the so-called presentation currency (currency in which the financial statements of an entity are presented) of the holding company (purchaser) at the spot rate at every closing date.

The example of Delhaize is a good illustration of the impact this can have. Delhaize reassessed the goodwill it had recognised when it acquired its American operations. The value of such goodwill, which had been calculated in euros under previous local GAAP, was restated to dollars (the functional currency of the American operations) at the date of transition and at every subsequent closing date as required by IFRS. This had a significant impact on Delhaize's opening IFRS balance sheet, resulting in a €269,9 million decrease in equity at 1 January 2003.

Where to from here?

The establishment of the opening IFRS balance sheet and restated 2004 financial statements under IFRS constituted the first step in the application of international financial reporting standards for the groups concerned.

The steps that follow will be influenced by the evolution of the IFRS framework, not only by changes to the existing standards and the publication of new ones but also by the choices of accounting policy, as well as interpretations to be made by groups in accounting for their future business combinations, in particular, the disclosure of the information required to be presented in the notes to the 2005 financial statements under IFRS.

Deloitte Touche Tohmatsu has a range of tools and publications to assist companies in implementing and reporting under International Financial Reporting Standards. These include:



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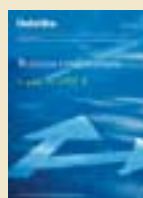
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