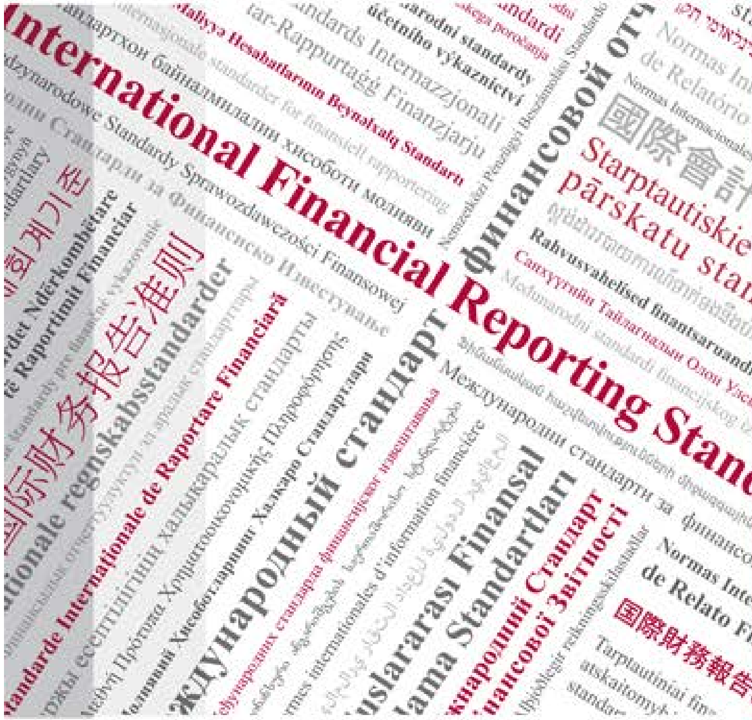
International Financial Reporting Standards



Goodwill and Impairment

Introduction

- A Post Implementation Review (PIR) is an important tool in ensuring that *IFRSs* are of high quality and relevant.
- The purpose of a PIR is to determine if: an *IFRS* is operating as intended; if it has achieved its objective and improved financial reporting; and to identify any unintended consequences or new issues which may have emerged.
- As required by our Due Process Handbook, the IASB recently completed a PIR of IFRS 3 *Business Combinations.*

Issues from the IFRS 3 PIR

- From this PIR, the IASB has identified two high priority issues:
  - improving impairment test in IAS 36 *Impairment of Assets*
  - subsequent accounting for goodwill
- Added to IASB research agenda in February 2015 together with two medium/high priority issues
  - identification and measurement of intangible assets
  - how to clarify definition of a business
- Discussions started at joint meeting with US FASB in September 2015

Source: *IFRS as global standards: (*updated July 2015, ongoing)

Addressing high priority issues in PIR

Area of focus	Possible next steps in the PIR report and feedback statement
Effectiveness and complexity of testing goodwill for impairment	Consider improvements/simplifications to the impairment model
Subsequent accounting for goodwill	Consider whether and how the costs of accounting for goodwill can be reduced without loss of information. Consider: • how improvements to impairment test could address some concerns raised • whether a variation on an amortisation and impairment model could be developed with an amortisation method that does not undermine the information currently provided by impairment-only approach.

What have we heard from investors?

- Some support current approach (non amortisation) as think has confirmatory value. Some reasons:
  - useful for relating price paid to what was acquired and for calculating return on invested capital
  - helps them to assess the stewardship of the management
  - helps them to verify whether an acquisition is working as expected

What have we heard from investors?

- Others want re-introduction of amortisation of goodwill. Some reasons:
  - acquired goodwill replaced by internally generated goodwill
  - estimating useful life no more difficult than for other intangibles
  - decreases volatility in profit or loss when compared to an impairment model
  - reduces pressure on identification of intangibles if goodwill and intangible assets amortised

Main challenges heard from preparers of impairment test

- Limitations of value in use calculation:
  - High degree of subjectivity
  - Difficulties in determining pre-tax discount rate
  - Prohibitions on what can be included in cash flows
- Time lag between impairment occurring and charge being recognised in the financial statements
- Costs/difficulties of annual impairment test and allocating/reallocating goodwill to CGUs

Suggestions for future academic research

- CEO Changes – what is the correlation of impairment charges when new CEO is an outside hire versus internal promotion?
- What is the correlation of impairment charges to announced changes in strategy versus other factors?
- Correlation of lagging entity share price movement versus overall equity market changes to incidences of impairment charges?
- What are the most relevant cash flows which should be included in impairment testing?
- In view of current IASB project agenda, increased research focus on goodwill impairments, and potential accounting alternatives, versus non goodwill impairments.