IFRS

STAFF PAPER

October 2018

IASB® Meeting

Project	**Goodwill and Impairment research project**		
Paper topic	Additional work to be performed		
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Purpose

1. The purpose of this paper is to ask the Board to confirm the further work to be performed on the research project prior to drafting the discussion paper. This paper does not discuss further work on disclosure, which is the subject of Agenda Paper 18B.

Structure of the paper

2. The paper is structured as follows:
   (a) background and introduction (paragraphs 3–7);
   (b) review of previous decisions made by the Board (paragraphs 8–12);
   (c) further work to be performed (paragraphs 13–27);
   (d) next steps (paragraphs 28–30); and
   (e) questions for the Board.

Background and introduction

3. In the July 2018 Board meeting, on the basis of the findings from the research project, the Board made the following tentative decisions:

(a) to pursue the objective of exploring whether disclosures could be improved to enable investors to assess more effectively whether a business combination was a good investment decision and whether the acquired business is performing after the acquisition as was expected at the time of the acquisition;

(b) to pursue the objective of simplifying the accounting for goodwill by exploring whether to:

(i) reintroduce amortisation; and/or

(ii) provide relief from the mandatory annual quantitative impairment testing of goodwill;

(c) to pursue the objective of improving the calculation of value in use (VIU) by removing from IAS 36 *Impairment of Assets*:

(i) the restriction that excludes from the calculation, those cash flows that are expected to result from a future restructuring or from a future enhancement; and

(ii) the requirement to use pre-tax inputs in the calculation.

4. At the same meeting, the Board tentatively decided:

(a) not to pursue the objective of removing the differences between accounting requirements for internally generated intangible assets and those for intangible assets acquired in a business combination;

(b) not to pursue the objective of changing the impairment testing model to focus on assessing whether the carrying amount of acquired goodwill is recoverable; and

(c) in pursuing the objective of simplifying the accounting for goodwill, not to consider requiring an entity to write-off goodwill immediately on initial recognition.

5. The Board also tentatively decided to issue a discussion paper as the research project's next step. The Board noted that this decision would not preclude it from issuing an exposure draft on, for example, targeted improvements to the value in use calculation.

6. The additional work to be performed to determine the improvements to disclosure requirements for business combinations, goodwill and impairment in relation to the research objective in paragraph 3(a) is discussed separately in Agenda Paper 18B.

7. This paper discusses the additional work to be performed in relation to the research objectives in paragraphs 3(b) and 3(c).

Review of previous decisions made by the Board

8. The decisions made in the July 2018 Board meeting included reconsidering some ideas that the Board had previously rejected and pursuing other ideas that the Board had already, during this research project, decided to explore.

9. Additionally, during the research project significant work had been performed in pursuing the objective of improving the effectiveness of the impairment testing model in IAS 36 by using the unrecognised headroom of a cash-generating unit (CGU) (or group of CGUs) as an additional input in the impairment testing of goodwill (the headroom approach). However, the Board decided in the July 2018 Board meeting not to pursue further the objective of improving the effectiveness of the impairment testing model.

10. Instead, the project has been set the objectives identified in paragraphs 3(a) –3(c). Some tentative decisions made by the Board earlier in this project were made in a context when the objectives of the project were different (for example, when the Board was exploring whether it was possible to make the impairment test more effective). Thus, the staff have assessed whether it would be appropriate for the Board to now reconsider any of those earlier tentative decisions in the context of the new objectives of the project.

11. The staff have assigned the tentative decisions made by the Board prior to the July 2018 Board meeting into six categories, as shown in the following table:

Original research objective	***Possible changes***	***The Board's initial decision prior to July 2018***	***Staff comments***
(a) Ideas the Board previously decided not to pursue and the staff do not propose the Board reconsider			
Improving the impairment test	Adding guidance on identifying CGUs and allocating goodwill to CGUs.	No specific decision made (December 2017)	This was explored as part of simplifying the impairment test. The staff thought that providing guidance on the allocation of goodwill that could apply to all entities would be difficult.
	Adding the pre-acquisition headroom as an additional input in the impairment test to improve the test's effectiveness.	No specific decision made (October 2017)	The pre-acquisition headroom approach was superseded by the updated headroom approach.
	Require any overpayment identified following the completion of the purchase price allocation to be identified and written off.	No specific decision made (March 2016)	The staff did not support this idea and the Board decided to focus on the pre-acquisition headroom approach.
	Measuring the acquired goodwill on a stand-alone basis against the assumptions that gave rise to it at acquisition.	No specific decision made (March 2016)	The staff did not support this idea and the Board decided to focus on the pre-acquisition headroom approach.
Subsequent accounting for goodwill	Accounting for separate components of goodwill.	No specific decision made (December 2017)	This would increase complexity of accounting for goodwill.
Recognising identifiable intangible assets in a business combination	Allow some identifiable intangible assets acquired in a business combination to be included within goodwill.	No (April 2018)	Not related to the new objectives.
	Remove the statement that an acquirer can always reliably measure the fair value of identifiable intangibles acquired in a business combination.	No specific decision made (November 2015)	This idea was considered early in the research project but was not included in the ideas which the Board considered in April 2018. This idea does not meet any of the new objectives set for the project in July 2018.
	Allow further grouping of intangible assets.	No specific decision made (November 2015)	This idea was considered early in the research project but was not included in the ideas which the Board considered in April 2018. This idea does not meet any of the new objectives set for the project in July 2018.

Original research objective	***Possible changes***	***The Board's initial decision prior to July 2018***	***Staff comments***
	Adding guidance for customer relationships, particularly regarding non-contractual customer relationships.	No specific decision made (November 2015)	This idea was considered early in the research project but was not included in the ideas which the Board considered in April 2018. This idea does not meet any of the new objectives set for the project in July 2018.
(b) Ideas the Board previously decided not to pursue and the staff propose the Board reconsider			
Improving the impairment test	Revisiting the methodology in the calculation of recoverable amount, mandating only one method (VIU or fair value less costs of disposal (FVLCD)) or requiring an entity to select the method that reflects the way the entity expects to recover the asset.	No (December 2017)	The idea has been considered both as a possible improvement to the effectiveness of the impairment test and as a simplification to the impairment test. The decision in December 2017 was made when the proposal was being considered as a possible improvement to the effectiveness of the impairment test.
	Allowing goodwill to be tested at the entity-level or at the level of a reportable segment.	No (December 2017)	This idea was rejected since it could lead to loss of information about impairment due to increased shielding.
	Adding guidance on the difference between VIU and FVLCD.	No specific decision made (December 2017)	This was explored as part of simplifying the impairment test although no specific decision was made. This was also mentioned in the recent October meeting of the Accounting Standards Advisory Forum (ASAF).
Recognising identifiable intangible assets in a business combination	Provide a further disaggregation of amortisation on the face of the statement of comprehensive income/income statement to allow investors to add back the amortisation of certain identifiable intangible assets.	No specific decision made (February 2016)	This idea was considered early in the research project but was not included in the ideas which the Board considered in April 2018. The Board decided in July 2018 not to pursue the objective of removing the differences between accounting requirements for internally generated intangible assets and those for intangible assets acquired in a business combination.
(c) Ideas the Board previously decided not to pursue that the Board decided in July 2018 to reconsider			
Improving the impairment test	Relief from the annual impairment test.	No (December 2017)	This had been considered under the objective of simplifying the impairment testing model. Four different approaches were analysed in December 2017.

Original research objective	***Possible changes***	***The Board's initial decision prior to July 2018***	***Staff comments***
Subsequent accounting for goodwill	Reintroduction of amortisation of goodwill.	No (December 2017)	
(d) Ideas the Board previously decided to pursue that the Board decided in July 2018 to continue to pursue			
Improving the impairment test	Simplifying the VIU calculation by reconsidering the use of pre-tax inputs.	Yes (January 2018)	
	Simplifying the VIU calculation by removing the prohibition on including restructuring and enhancing cash flows.	Yes (January/May 2018)	
(e) Ideas the Board previously decided not to pursue that the Board decided in July 2018 to continue not to pursue			
Subsequent accounting for goodwill	Direct write-off of goodwill to profit or loss, other comprehensive income or equity.	No specific decision made (December 2017)	In Agenda Paper 18B for the December 2017 Board meeting and in Agenda Paper 18B for the February 2016 Board meeting, the staff explained why they did not support direct write-off. No specific decision was made by the Board until July 2018 when the Board decided not to pursue this idea.
(f) Ideas the Board previously decided to pursue that the Board decided in July 2018 not to pursue			
Improving the impairment test	Adding updated headroom as an additional input into the impairment test to improve the test's effectiveness.	Yes (December 2017)	

12. The staff have summarised the further work that it considers is required to be performed prior to drafting a discussion paper for those ideas identified in paragraph 11(b), if the Board agreed to reconsider those ideas, and in paragraphs 11(c)–11(d). This is further discussed in the next section.

Further work to be performed

Simplification of the impairment test

13. At the July 2018 Board meeting, the Board set an objective to consider improving the calculation of VIU by removing from IAS 36:

(a) the restriction that excludes from the calculation cash flows that are expected to result from a future restructuring or from a future enhancement; and

(b) the requirement to use pre-tax inputs in the calculation.

14. Both amendments would simplify the impairment test and were explored fully in Agenda Papers 18A and 18B for the January 2018 Board meeting and feedback on the proposals has been received from the ASAF and the Global Preparers Forum (GPF). In the staff's view no further work would be required on these ideas prior to drafting a discussion paper.

15. The amendments identified in paragraph 13 would reduce the differences between an asset's (or CGU's) VIU and FVLCD. If recoverable amount remained defined as the higher of an asset's (or CGU's) VIU and FVLCD, the Board could consider proving guidance on the differences between the two methods. Indeed, two ASAF members at the recent October meeting of the ASAF suggested such guidance would be needed. Agenda Paper 18C for the December 2017 Board meeting contains analysis of the similarities and differences between VIU and FVLCD which could form the basis of this guidance, but the staff think that feedback on the guidance should be sought from the Board's consultative groups prior to inclusion in a discussion paper if the Board decided to pursue this idea.

16. At the same meeting, one ASAF member also suggested that the Board should consider further ways to simplify the impairment test beyond the amendments described in paragraph 13 and that member was conducting research on ways to simplify the impairment test.

17. The Board could investigate further ways to simplify the impairment test by:

(a) conducting its own research;

(b) considering the results of the research conducted by the ASAF member;

(c) considering whether to adopt a single method for determining recoverable amount (see paragraph 18); and/or

(d) considering whether to allow goodwill to be tested at the entity-level or at the level of a reportable segment (see paragraph 19).

18. The Board explored whether to adopt a single method for determining recoverable amount as a means of improving the effectiveness of impairment testing of goodwill. The Board rejected this approach, deciding to instead explore further improvements to the impairment test by using the unrecognised headroom as an additional input in the impairment testing of goodwill. Adopting a single method for determining recoverable amount is also a possible simplification of the impairment test and this could be investigated further. This proposal was explored fully in Agenda Papers 18C for the December 2017 Board meeting and feedback on the proposal has been received from the ASAF and GPF. In the staff's view no further work would be required on this idea prior to drafting a discussion paper.

19. The Board considered allowing goodwill to be tested at an entity-level or at the level of a reportable segment. This was discussed in Agenda Paper 18E for the December 2017 Board meeting. The staff did not recommend this idea because it could have led to loss of information about impairment due to increased shielding and this was not compatible with the Board's objective at that time of exploring how to make the impairment test more effective. The Board could now consider this simplification, but further work would need to be performed to develop this further.

Simplifying the accounting for goodwill

20. At the July 2018 Board meeting, the Board set an objective of simplifying the accounting for goodwill by exploring whether to:

    (a) reintroduce amortisation; and/or

    (b) provide relief from the mandatory annual quantitative impairment testing of goodwill.

21. Agenda Paper 18B for the December 2017 Board meeting and Agenda Paper 18C for the June 2018 joint meeting of the Board and the FASB sets out the Board's discussions on amortisation.

22. If the Board did consider reintroducing amortisation the Board would also have to consider:

    (a) the useful life of goodwill;

(b) the amortisation method;

(c) whether indefinite life intangible assets should be amortised;

(d) the allocation of impairment to amortised goodwill;

(e) the allocation of amortised goodwill on disposal; and

(f) the potential transition requirements.

23. The issues in paragraphs 22(a)–22(e) were considered in detail in Agenda Paper 18B for the February 2016 meeting of the Board.

24. In the staff's view the Board could consider the following further work on amortisation:

(a) Seek feedback from ASAF, GPF and the Capital Markets Advisory Committee (CMAC) to confirm the feedback we have heard during the project from preparers and investors on amortisation and to obtain feedback on the issues in paragraph 22.

(b) Since amortisation might at least partially mitigate concerns that the current impairment testing model does not focus on the carrying amount of acquired goodwill, seek feedback from investors through the CMAC and outreach to a wider selection of investors on what the carrying amount of goodwill is used for and whether investors believe it is a problem that acquired goodwill is, arguably, gradually replaced by internally generated goodwill.

25. If amortisation is not reintroduced, but there is still concern over the carrying amount of goodwill, the Board could consider requiring additional disclosure to highlight the amount of an entity's reported equity that arises from the recognition of goodwill.

26. This requirement could be extended to disclosure of the amount of equity an entity would report if it did not recognise goodwill and those acquired intangible assets that would not have been recognised if they had been internally generated and to disclose the profit or loss an entity would report without amortisation and without any impairment losses on those intangible assets and on goodwill. Some argue that this idea could allow investors to better compare the performance of entities growing organically with entities growing through acquisitions.

27. Agenda Paper 18E for the December 2017 Board meeting considered the possible relief from the mandatory annual quantitative impairment test and staff analysed four approaches that could be considered. Feedback on these approaches was obtained from ASAF, GPF and CMAC. In the staff's view no further work would be required on this idea prior to drafting a discussion paper.

Next steps

28. Subject to the decisions taken by the Board on the additional work to be performed on the project prior to drafting a discussion paper, the staff expect to present the findings of that additional work at a Board meeting or meetings in H1 2019.

29. Based on this additional work and previous work performed during the project, the staff intend to present a package of possible solutions for the Board to consider with analysis of how the solutions meet the objectives set by the Board in July 2018.

30. The staff would then ask for permission to prepare a ballot draft of a discussion paper at a subsequent Board meeting. At the same time, the Board will also consider whether certain of the possible solutions would be included in an exposure draft. The staff would therefore expect a discussion paper to be able to be issued during H1 2020.

Questions for the Board

1. Does the Board agree to the additional work detailed in paragraphs 15, 17 and 24 to 26 to be performed prior to drafting a discussion paper?

    a. paragraph 15 – develop guidance on the differences between VIU and FVLCD;

    b. paragraph 17 – further simplification of the impairment test by:

        i. conducting its own research

        ii. considering the results of the research conducted by the ASAF member;

iii. considering whether to adopt a single method for determining recoverable amount; and

iv. considering whether to allow goodwill to be tested at the entity-level or at the level of a reportable segment;

c. paragraph 24(a) – seek feedback from consultative groups on amortisation;

d. paragraph 24(b) – seek feedback from investors on what the carrying amount of goodwill is used for; and/or

e. paragraphs 25 to 26 – disclosure of reported equity and profit or loss adjusted for acquired intangible assets that would not have been recognised if internally generated and goodwill.

2. Does the Board have any further suggestions for additional work for the staff to perform prior to drafting a discussion paper?