

STAFF PAPER

November 2015

IASB Meeting

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| Project | Goodwill and impairment project | | |
| Paper topic | Feedback from users of financial statements about information on goodwill and impairment | | |
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This paper has been prepared for discussion at a public meeting of the IASB and does not represent the views of the IASB or any individual member of the IASB. Comments on the application of IFRSs do not purport to set out acceptable or unacceptable application of IFRSs. Technical decisions are made in public and reported in IASB *Update*.

Accounting Standards Advisory Forum, December 2015, Agenda paper 5E**Objective of this paper**

1. The purpose of this agenda paper is to:
 - (a) summarise the feedback we have heard so far from users of financial statements to help us assess what information they want to receive about goodwill and impairment; and
 - (b) ask the IASB what additional feedback they would like in this area.

Structure of this paper

2. This paper includes the following sections:
 - (a) Introduction
 - (b) Staff summary of the main feedback
 - (c) Agenda for the November 2015 CMAC meeting
 - (d) Staff observations so far
 - (e) Questions for the IASB
 - (f) The staff have provided the following four appendices for IASB member's reference when reading this agenda paper (these are provided in a separate agenda paper—see Agenda Paper 18C):

- (i) Appendix E: Relevant extracts from comment letter analysis on the Post-implementation Review (PIR) of IFRS 3 *Business Combinations*
- (ii) Appendix F: Relevant extracts from past Capital Markets Advisory Committee (CMAC) meeting summaries
- (iii) Appendix G: User outreach performed by the FASB
- (iv) Appendix H: Some history behind the development of the requirements for accounting for goodwill

Introduction

3. The IASB’s report and feedback statement on the PIR of IFRS 3 noted that there are mixed views amongst investors and other users of financial statements about accounting for goodwill and impairment. Some support the current requirements (ie the impairment-only approach). The following are the main reasons in the report:

- (a) it is useful for relating the price paid to what was acquired and for calculating the return on invested capital;
- (b) it helps them to assess the stewardship of the management; and
- (c) it helps them to verify whether an acquisition is working as expected.

They think that the information provided by the impairment test of goodwill is useful, because it has confirmatory value.

4. However others said they would prefer the re-introduction of the amortisation of goodwill. The following are the main reasons in the report:

- (a) goodwill acquired in a business combination is supported and replaced by internally generated goodwill over time;
- (b) estimating the useful life of goodwill is possible and is no more difficult than estimating the useful life of other intangible assets;
- (c) goodwill has been paid for and so, sooner or later, it should have an impact on profit or loss;
- (d) amortising goodwill would decrease volatility in profit or loss when compared to an impairment model; and

- (e) amortising goodwill would reduce pressure on the identification of intangible assets.
5. At its meeting in October 2015, some IASB members said they would like more feedback from users to help them understand better what information users want to receive about goodwill and impairment and also see how they currently use the information about goodwill and impairment provided by companies. This paper summarises what we know so far to inform the IASB’s discussion and help us decide what additional feedback we need.

Staff summary of the main feedback

6. In preparing this agenda paper the staff have reviewed:
- (a) the comment letters received on the PIR from users of financial statements (extracts from the comment letter analysis presented to the IASB at its September 2014 meeting are in Appendix E).
 - (b) feedback received from past meetings with the Capital Markets Advisory Committee (extracts from past CMAC meeting summaries where goodwill and impairment were discussed are in Appendix F).
 - (c) internal staff summaries of feedback from individual meetings and conference calls that staff held with users during the PIR (includes meetings and/or conference calls with several analysts (debt and equity analysts, mainly buy side), individual members of the Corporate Reporting Users’ Forum (CRUF) and Capital Markets Advisory Committee (CMAC); CFA Institute (International and UK branches); EFRAG User Panel; User Advisory Council (UAC) of the Canadian Accounting Standards Board (AcSB); and European Federation of Financial Analysts Societies (EFFAS)).
 - (d) The summary of the findings of FASB staff during their outreach with users of public business entities that was presented to the IASB and FASB in September 2015 (included in Appendix G).

7. Based on our review of the sources in paragraph 6, the staff think the following are the key messages we have heard so far about what information users want to receive about goodwill and impairment and how they use the current information:

(a) Some users have told us they would like amortisation of goodwill to be reintroduced. However, we and the FASB have received consistent feedback that the majority of users think:

(i) the impairment-only approach provides them with more relevant information; and

(ii) amortisation of goodwill over an arbitrary period does not provide decision useful information.

(b) Although some users support reintroducing amortisation, their reasoning generally seems to be based on:

(i) conceptual arguments (eg because goodwill is replaced by internally generated goodwill over time) and/or

(ii) because information provided by an impairment-only approach has limited use (see paragraph (d)).

rather than because they think amortisation with impairment would provide them with better information than an impairment only approach. Although some thought that knowing management's assessment of the useful life of goodwill may be informative.

(c) Users appear to be particularly interested in assessing whether an acquisition has been successful, identifying what assumptions and projections formed the basis for the valuation (and hence support the goodwill figure) and assessing the accountability of management. Currently users seem to find information about goodwill and impairment primarily helpful in assessing the accountability of management (eg whether management overpaid and if the acquisition was a good business decision).

(d) Many users say information provided under the current requirements has limitations for the following main reasons:

(i) impairment losses are recognised too late.

- (ii) impairment calculations are inherently very judgemental and the assumptions used in the calculations are subjective.
- (iii) disclosures are not sufficient to assess whether the main inputs/assumptions are reasonable. However some users said that some disclosures are useful, these included discount rates used, long-term growth rates, profit and capital expenditure assumptions and sensitivities.
- (iv) insufficient information to help them understand the subsequent performance of the acquired business and whether main targets/synergies of the acquisition are met, considered key to their analysis.

Some users focus more on the timing of the impairment write down and the overall magnitude rather than the actual amount of impairment recognised.

- (e) The feedback in paragraphs (c)-(d) seems consistent with some of the feedback from the FASB outreach that goodwill impairment is often more helpful qualitatively, rather than being used and relied on quantitatively.

Agenda for the November 2015 CMAC meeting

8. In order to understand better what information investors want to receive about goodwill and impairment, a thirty minute session has been added to the November Capital Markets Advisory Committee (CMAC) meeting agenda on 6 November 2015.
9. As the length of the session is short the session will focus on questions that will help the IASB understand CMAC members' views on goodwill amortisation and how users currently use the information provided by entities about goodwill and impairment—for example whether users currently make any adjustments to the information provided by companies. This will help to inform the IASB's discussion on whether to consider reintroducing amortisation and what improvements can be made to the impairment requirements.
10. At the time of preparing this paper, the meeting had not yet taken place. Consequently, the staff will provide IASB members with an oral overview of the feedback from CMAC members at this November IASB meeting.

Staff observations so far

11. Users have told us that whilst the current information about impairments is useful, impairment losses are recognised too late, that the impairment test is judgemental, and assumptions are subjective and insufficiently disclosed. The staff think that even if we identify ways to improve the impairment test and the test is better applied and disclosed, any impairment test of goodwill is likely to be inherently subjective.

12. Consequently the staff think that preparers and users may be served better by the following (this is in line with the suggestions made by the staff in Agenda Paper 18B for the October 2015 meeting):
 - (a) Not reintroducing amortisation for goodwill, but focussing on making the impairment test less burdensome to apply (for example by introducing an indicator-only test for goodwill rather than the annual requirement) and considering if we can streamline the existing disclosure requirements. The staff think this could provide relief for preparers on one hand without significant loss of information for users.

 - (b) Requiring some kind of disclosure to help users assess the subsequent performance of the acquiree during the first 12-24 months following the acquisition. The staff think that even in cases where the acquiree is integrated into the acquirer's business it should be possible for the acquirer to provide information on:
 - (i) the key performance assumptions or targets (indicators) supporting the purchase price (for example revenue targets, operating margins, cost savings etc), and hence those indicators supporting the goodwill figure.

 - (ii) a basic comparison of actual performance against the expected indicators in the first 12-24 months following acquisition.

13. We have had feedback that the disclosure requirements in IFRS 3 and IAS 36 *Impairment of Assets* are already excessive. Furthermore, some preparers also say that it is difficult to provide information about the subsequent performance of the acquiree, particularly if the acquiree is integrated into the acquirer's business or if the acquirer makes many acquisitions over a period of time. However if we also consider ways to

simplify the current impairment testing requirements, the staff think the approach in paragraph 12 would be unlikely to lead to a net additional cost or complexity for preparers and should provide better information to users. Moreover, the staff think that as stewards of the entity, management is responsible for ensuring that the progress of an acquisition is measured and compared to the assumptions used to determine the price paid for it.

14. The staff think that even in cases where an acquiree is integrated immediately and tracking information over 24 months is difficult, some information could still be tracked and/or provided for a shorter period. Furthermore, the staff think that such cases should not prevent us from considering this disclosure for all acquisitions.
15. The staff note that considering information about the subsequent performance of the acquiree was listed in the PIR as of medium significance and has not yet been added to the IASB's agenda. It was decided that depending on the feedback received from the 2015 Agenda Consultation, we could investigate whether it would be practical to prepare this information, and for how many reporting periods it would be cost-beneficial. However the staff note that providing subsequent information can take many forms, from requiring detailed financial information/financial statements to disclosures about key financial indicators. The staff has limited its consideration to the latter. Nevertheless, IASB members may think we should address disclosure of this type of information separately from this goodwill and impairment project.

Questions for the IASB

Questions

- 1) After considering the summary of feedback received from users in this paper and feedback from CMAC members at their November meeting, what additional information would IASB members like to know about what investors want to receive about goodwill and impairment?
- 2) Do IASB members think we should consider addressing any disclosures about subsequent performance of the acquired business, for example about whether the key targets/synergies of the acquisition are met, as part of this project?

[Appendices E-H are in Agenda Paper 18C]