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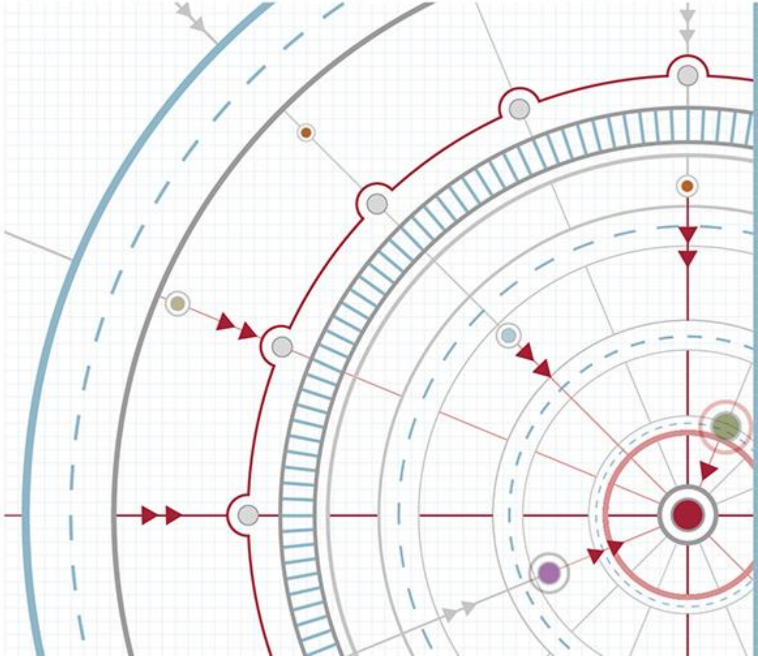

Joint CMAC–GPF meeting, 15–16 June 2017

Agenda Paper 5A

Impairment testing of goodwill

Raghava Tirumala | rtirumala@ifrs.org | +44 (0)20 7246 6953

Woung Hee Lee | wlee@ifrs.org | +44 (0)20 7246 6947

Appendices accompanying this paper are included in Agenda Paper 5B

Agenda

Objectives of Goodwill and Impairment research project

Objectives of the research project

Whether it is possible to:

- Improve the quality of information provided to users without imposing costs that outweigh benefits
- Simplify and improve application of impairment test without loss of information to investors

Why improve the quality of information?

IAS 36 requirements

- Goodwill is allocated to cash generating unit(s) for impairment testing purposes
- This is not necessarily at the level of the acquired entity as a whole

Investors' concerns

- Insufficient information about subsequent performance of the acquired business

Ongoing research

- Additional disclosures that help investors understand subsequent performance of acquired businesses

- Pages 12–15

Why simplify the impairment test?

IAS 36 requirements

- Goodwill is not amortised
- Quantitative impairment testing annually and whenever there is an indication of impairment
- Recoverable amount* to be calculated every year

Preparers' concerns

- Performing the test annually is costly

Ongoing research

- Relief from mandatory annual quantitative test
- Calculating recoverable amount when there are indicators of impairment
- Pages 16–21

* Recoverable amount is higher of fair value less costs of disposal (FVLCD) and value in use (VIU)

Past discussions with CMAC and GPF

Past discussions with CMAC and GPF

- Three meetings—one with CMAC and two with GPF
- Additional disclosures were the focus of all three meetings
- Feedback (see pages 9–11) considered in developing possible additional disclosures that the Board could require
- Agenda Paper 18D of May 2017 Board meeting reflects the latest thinking of staff (see page 13)

Feedback from CMAC

Month	Questions asked	Summary of feedback
November 2015 (link to the agenda paper)	Do you make any 'non-GAAP' adjustments to goodwill or impairment for your analysis?	• Impairment charge generally added back only for determining cash flows • That does not mean that analysts disregard impairment charge or consider that information unhelpful
	Would amortisation of goodwill help or hinder you analysis?	• Mixed feedback about amortisation of goodwill • Current impairment test provides useful information • Impairment test should be made robust rather than introducing other approaches
	Is there any other information that you need for your analysis?	• Additional disclosures to help investors understand the key drivers that justified the purchase consideration • Breakdown of carrying amount of goodwill by past acquisitions
		Click the links for full meeting summary and recording.

Feedback from GPF

Month	Questions asked	Summary of feedback
March 2016 (link to the agenda paper)	In developing disclosures about key assumptions or targets supporting the purchase consideration and comparison of actual performance vis-à-vis targets, what information would be meaningful and possible to prepare?	• In respect of the key assumptions or targets: – Disclosing sensitive key targets could give away an entity's competitive advantage – Some key targets may not be measurable and auditable, eg acquisition of human competencies – Disclosure of components of goodwill is already required and that information is sufficient • In respect of actual performance vis-à-vis the targets: – It is difficult to track actual performance when acquired business is integrated with existing business – Not meeting the targets does not necessarily mean that the acquisition is not successful
		Click the links for full meeting notes and recording.

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Feedback from GPF (continued)

Month	Questions asked	Summary of feedback
March 2017 (link to the agenda paper)	Feedback on the following possible simplifications to the impairment test of goodwill: • Using either FVLCD or VIU as the sole basis for calculating recoverable amount • Relief from annual testing • Relaxing some restrictions on cash flows included in VIU calculations • Additional guidance on applying IAS 36	• Several members favoured relief from annual testing and relaxing the restrictions on cash flows included in VIU calculations • In relation to using either FVLCD or VIU as the sole basis for calculating recoverable amount, some members indicated a preference for a model that uses VIU
		Click the links for full meeting notes and recording.

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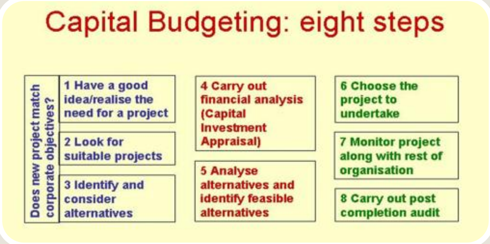
Additional disclosures about acquired businesses

Staff current thoughts—disclosures



Key assumptions or targets supporting the purchase consideration

(these disclosures follow on from management's own assessment and communications to external stakeholders at the time of acquisition)

Comparison of actual performance vis-à-vis assumptions made at the time of acquisition

(the number of years for which a company will disclose this comparison will depend upon the time horizon set by the company at the time of acquisition)

Breakdown of goodwill by past acquisition

(the Board could additionally require reconciliation of this disaggregation with the existing requirement to disclose goodwill allocated to cash-generating unit(s))

See Appendix 1 of this paper for a summary of Agenda Paper 18D of May 2017 Board meeting

Staff current thoughts—disclosures
(continued)

- Additionally, existing disclosure requirements in IAS 36 could be reviewed to assess if any disclosures are not useful*
- Some feedback from GPF members that:
  - disclosure of pre-tax discount rate is not useful because post-tax discount rates are generally used in calculating value in use
  - disclosing sensitivity analysis should be removed because those disclosures make it easy to derive an entity’s budgets

* *See Appendix 2 of this paper for extract of paragraphs 134–137 of IAS 36 that contain requirements about disclosure of estimates used to measure recoverable amounts of cash-generating units containing goodwill*

Questions to CMAC–GPF

- Do you have any comments or feedback about the possible additional disclosures explained in page 13?
- Do you think any of the existing disclosure requirements in IAS 36 are not useful (see page 14 and Appendix 2)?

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Indicator-only approach to goodwill impairment testing

Staff current thoughts—indicator approach

Date of acquisition

Approach 1

Complete relief from mandatory annual test—Goodwill tested for impairment only when there is an indication of possible impairment

Approach 2

Partial (less constrained) relief from annual testing— Mandatory quantitative test for the first year after acquisition and indicator-based impairment test in later years

Approach 3

Partial (more constrained) relief from annual testing—Mandatory quantitative test for the first few years after acquisition and indicator-based impairment test in later years (the Board could require the test to be performed for 3–5 years)

Year 1 | Year 2 | Year 3 | Year 4 | Year 5 | Year 6

Staff current thoughts—indicator approach

(continued)

Indicators of impairment

- IAS 36 provides a list of indicators that an entity must consider as a minimum (see page 20)
- The following additional indicators could be added:
  - Actual performance not in line with the key performance assumptions or targets supporting the acquired goodwill

Staff current thoughts—indicator approach
(continued)

Consequences of introducing indicator-only approach

- Cost and complexity of goodwill impairment test are reduced
- Inputs to the quantitative test currently disclosed every year will be disclosed only when there is an impairment loss
- Questions about timely recognition of impairment might arise
- Success of the approach depends upon proper application of the Standard and the audit and enforcement framework

Indicators currently listed in IAS 36

External information (¶12 of IAS 36)	Internal information (¶12 of IAS 36)	Internal reporting (¶14 of IAS 36)
• Observable indications that asset's value has significantly declined • Significant changes with an adverse effect in the technological, market, economic, or legal environment • Market interest rates have increased, affecting discount rate • Carrying amount of net assets is more than its market capitalisation	• Obsolescence or physical damage of an asset • Significant changes with an adverse effect on selling or using an asset • Economic performance of an asset is worse than expected	• Cash flows for acquiring and operating the asset is higher than budgeted • Actual net cash flows or operating profit from asset are worse than budgeted • A significant decline in budgeted cash flows or operating profit from asset • Operating loss or net cash outflows for the asset

See Appendix 2 of this paper for extract of paragraphs 7–17 of IAS 36

Questions to CMAC–GPF

- Do you have any concerns about the relief from annual test?
- Which relief approach on page 17 would you prefer and why?
- Could you suggest any indicators that could be added to the list in IAS 36, especially indicators of overpayment?
- The existing internal reporting indicators (see page 20) are financial indicators. Do you think there could be non-financial indicators of impairment?

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