IFRS® Foundation

Business Combinations—Disclosures, Goodwill and Impairment

Capital Markets Advisory Committee
Agenda Paper AP2
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Agenda

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Purpose of this session

Background

- Board is considering feedback to the Discussion Paper *Business Combinations—Disclosures, Goodwill and Impairment* published in March 2020

Purpose of this session

- To seek CMAC members' views on the:
  - business combinations investors need subsequent performance information about;
  - usefulness of an amortisation model based on management's expectations of the useful life of goodwill; and
  - how difficult investors would find a comparison of financial statements if IFRS Standards and US GAAP had different requirements for goodwill.

Project background

Goodwill and Impairment

2013–2015	2015–2019	Q1 2020	Q2–Q4 2020	2021–Q1 2022
IFRS 3 Post-implementation Review	Development of Discussion Paper	Discussion Paper published	Consultation period	Feedback summary and initial analysis

Objective

- Improve information companies provide about their acquisitions

Preliminary views

1
- Disclose management's objectives for acquisitions and subsequently disclose the performance against those objectives
- Some targeted improvements to existing requirements

2
- Retain impairment-only model for goodwill
- Simplify impairment test

3
- Present amount of total equity excluding goodwill
- Do not change recognition of intangibles separately from goodwill

What is the Board investigating?

- In June 2021, the Board tentatively decided to retain the objective of the project unchanged from that described in the Discussion Paper. The objective is to explore whether companies can, at a reasonable cost, provide investors with more useful information about the acquisitions those companies make. The Board also tentatively decided to make no changes to the project scope. The Board views its preliminary views as a package that meets the project objective.

- The Board decided on a project plan at its meeting in September 2021. As part of that project plan the Board is prioritising analysis of feedback on:
  - disclosures about business combinations; and
  - whether to retain the impairment-only model or whether to reintroduce amortisation for goodwill (the subsequent accounting for goodwill).

- The Board plans to:
  - make tentative decisions about disclosures to help the Board get a better understanding of the disclosure package it could develop; and
  - research particular aspects of the feedback on the subsequent accounting for goodwill.

- This analysis will help the Board decide on the subsequent accounting for goodwill. The Board is not currently developing an amortisation model.

Disclosures about business combinations

The Board’s preliminary view

The Board’s preliminary view

- Require companies to disclose in the year of a business combination the strategic rationale and objectives for the acquisition and the metrics management plan to use to monitor achievement of those objectives.
- In subsequent years require a company to disclose performance against those objectives.
- The Board’s Standard on business combinations already requires an entity to disclose information about business combinations. Disclosure is required individually for all business combinations for which information is material.
- In developing the Discussion Paper, the Board heard that requiring disclosure of subsequent performance for all those business combinations might be costly.
- The Board’s preliminary view is to require companies to disclose information about business combinations reviewed by management. Management would be defined using the concept of the Chief Operating Decision Maker (CODM) from the Standard on operating segments. Often the CODM is the CEO or COO but it maybe a group of executive directors or others.
- The Board expects such an approach to result in disclosure of the most important information about the most important business combinations.

Feedback on the preliminary view

Feedback on the Discussion Paper

- Many respondents said using the CODM to identify business combinations is a practical approach that provides a reasonable cost-benefit balance.
- However, some respondents said the CODM monitors only the most significant business combinations and that the Board's preliminary view would result in investors not receiving information about all the business combinations that matter to investors—the population of business combinations for which an entity is already required to disclose information.
- A few respondents, including a few investors, suggested requiring disclosure of subsequent performance of only 'significant' or 'fundamental' business combinations—perhaps using a quantitative threshold, for example the size of the acquired business as a percentage of the entity's revenue or market capitalisation.

Next steps

What is the Board investigating?	
What is the Board investigating?	• As a result of the feedback, the Board is researching the population of business combinations for which investors need subsequent performance information. • This information will help the Board to understand whether to continue with its preliminary view or whether to identify a different population of business combinations for which to require disclosures about. • In particular, the Board is asking whether investors require subsequent performance information about: a) all business combinations for which they currently receive information about in the financial statements on an individual basis; or b) a subset of those business combinations. • If investors need this information for only a subset of business combinations, what business combinations are included in that subset?

Disclosures about business combinations—Questions for CMAC members

Questions on topic 1

- Do you need subsequent performance information about all business combinations for which you currently receive information in financial statements in the year of acquisition on an individual basis or is that information needed for only a subset of those business combinations?
- If you need subsequent performance information for only a subset of business combinations, how would you define that subset?

Subsequent accounting for goodwill

Background

Basis for conclusions on IAS 36 (2004)	• The Board observed that the useful life of acquired goodwill and the pattern in which it diminishes generally are not possible to predict, yet its amortisation depends on such predictions. As a result, the amount amortised in any given period can be described as at best an arbitrary estimate of the consumption of acquired goodwill during that period. • The Board said that if a rigorous and operational impairment test could be devised, more useful information would be provided under an approach in which goodwill is not amortised, but is instead tested for impairment annually (or more frequently if events or changes in circumstances indicate that the goodwill might be impaired).

The Board's preliminary view	• Retain the impairment-only model

Feedback

Feedback on the Discussion Paper

- Some respondents favouring reintroducing amortisation said entities can reliably estimate goodwill's useful life. Although most acknowledged the challenges of doing so, they said doing so would be no more challenging than estimating the useful life of other tangible and intangible assets.
- Many of these respondents, a few of whom were investors, said judgements about the useful life of goodwill could provide useful information about the period over which management expects to realise benefits associated with goodwill.
- Some respondents said companies would have information from the acquisition process (for example, estimates of synergies and payback periods) that could allow management to reasonably estimate goodwill's useful life.
- In addition, one investor said amortising goodwill would help management and investors evaluate performance because the resulting amortisation expense would be matched against revenue generated by the business combination.

Next steps

What is the Board investigating?

- In 2004, when moving to an impairment-only model, the Board noted that respondents to the Exposure Draft generally accepted that ‘the useful life of acquired goodwill cannot be predicted with a satisfactory level of reliability, nor can the pattern in which that goodwill diminishes be known.’
- Feedback to the Discussion Paper was more mixed than in 2004, which indicates a possible shift in stakeholder views.
- The Board is therefore investigating how feasible it is to estimate a useful life of goodwill and how useful that information would be. This is part of the Board’s work on considering whether to retain the impairment-only model to account for goodwill or to reintroduce amortisation of goodwill.
- If the Board were to reintroduce amortisation of goodwill, companies would still need to perform an impairment test and therefore a company might still provide information about impairments in particular circumstances.
- In an amortisation based model, information could be provided by:
  - disclosures about management’s estimates of the life of goodwill; and/or
  - the amortisation expense recognised in the financial statements.

Subsequent accounting for goodwill—Questions for CMAC members

Questions on topic 2

- Would an amortisation model in which a company would be required to amortise goodwill based on management's estimate of the useful life of goodwill (in which companies would still be required to perform an impairment test—an amortisation and impairment model) provide useful information?
- If so, what information would be useful in this amortisation and impairment model? For example, is management's estimate of the useful life of goodwill the only additional piece of useful information or would the amortisation expense in profit or loss also provide useful information and why?
- What information would investors lose, if any, if the Board were to require the application of this amortisation and impairment model? Would the information gained from understanding management's estimate of the useful life of goodwill compensate for the information lost?

Convergence with US GAAP

Background and next steps

Background	• IFRS Standards and US Generally Accepted Accounting Principles (US GAAP) both currently require an entity to apply an impairment-only model to account for goodwill. The details of the impairment models in the respective frameworks have some differences but are largely converged. • The US Financial Accounting Standards Board (FASB) is also considering the accounting for goodwill. • The Board's preliminary view is to retain the impairment-only model to accounting for goodwill. However, the FASB have tentatively decided to reintroduce amortisation of goodwill.

What is the Board investigating?	• If divergence in the accounting for goodwill between IFRS Standards and US GAAP were to exist, the Board is considering:
	  • how investors would compare financial statements of entities applying different accounting frameworks;
	  • whether investors would have difficulties in comparing financial statements in such circumstances and if so, why; and
	  • what additional information investors would need to compare financial statements of entities applying different accounting models to goodwill.

Convergence with US GAAP—Questions for CMAC

Questions on topic 3

- If the Board and FASB were to require entities to account for goodwill differently:
  - How would you compare financial statements of entities that applied an impairment-only model for goodwill to financial statements of entities that amortised goodwill? For example, would you start with financial statements of entities that amortise goodwill and make adjustments to make them comparable to financial statements of entities applying an impairment-only model or vice versa?
    - Please explain whether and how this analysis would differ from your current analysis, particularly if you currently add back impairment expenses or would add back an amortisation expense.
  - What additional information, if any, would you need to compare financial statements prepared applying different accounting models for goodwill?

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