IFRS
Accounting

Goodwill and Impairment

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Agenda

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Background

Background

Objective

To improve the information entities provide to users of financial statements (users), at a reasonable cost, about the business combinations those entities make.

Path forward

The IASB is redeliberating its preliminary views in the Discussion Paper and will make tentative decisions on whether to:

- retain or amend those preliminary views in the light of feedback; and
- move forward with standard-setting and publish an exposure draft.

Project History

2013–2015	March 2020	March 2021—Present	TBD
PIR of IFRS 3	Discussion Paper	Project Redeliberation	Potential Exposure Draft

Discussion Paper—The IASB’s preliminary views

1 Improving disclosures about business combinations	Require entities to disclose: • management’s key objectives for business combinations; and • how business combinations subsequently perform. Some targeted improvements to existing disclosures, notably to require entities to disclose quantitative information about expected synergies.	
2 Improving the accounting for goodwill	A Can the impairment test be made more effective?	Not significantly, and not at a reasonable cost.
	B Should goodwill be amortised?	No, retain the impairment-only model.
	C Can the impairment test be simplified?	Yes, provide relief from the annual impairment test and simplify value in use.
3 Other topics	• Present on the balance sheet the amount of total equity excluding goodwill. • Do not change recognition of intangible assets separately from goodwill.	

Since the Discussion Paper

March-May 2021

The IASB reviews feedback on the Discussion Paper

June 2021

The IASB tentatively decides to retain the objective and scope of the project

September 2021

The IASB decides to prioritise analysis on:

- disclosures about business combinations; and
- specific aspects of feedback on whether to retain the impairment-only model or whether to reintroduce amortisation for goodwill

September 2022

The IASB tentatively decides whether to proceed with disclosure preliminary views

Q4 2022

The IASB to tentatively decide on:

- whether to explore reintroducing amortisation of goodwill; and
- whether to move the project from the research to standard-setting phase

After Q4 2022 the IASB will make tentative decisions on other aspects of the project

Updates

➊ Improving disclosures about business combinations

In this section

The preliminary views

Additional disclosure objectives

- Add additional disclosure objectives to IFRS 3 *Business Combinations* that would require entities to disclose information that would help users understand:
  - the benefits an entity expected from a business combination when agreeing the price to acquire that business; and
  - the extent to which management's objectives are being met.

Disclosure about performance of business combinations

- Require entities to disclose in the year of a business combination, the strategic rationale and objectives for that business combination and the metrics management plan to use to monitor achievement of those objectives.
- In subsequent years, disclose management's review of the entity's performance against those objectives (actual performance).
- The information that would be disclosed is the information an entity's Chief Operating Decision Maker (CODM) is reviewing to assess the performance of the business combinations that the CODM is reviewing.

Disclosure about expected synergies

- Require entities to disclose in the year of a business combination quantitative information about the synergies expected as a result of the business combination.

The preliminary views—staff examples

Westferry's disclosure for the year ended 31 Dec 20X5 (Year of acquisition)

Strategic rationale	**Information about the business combination** • The Group acquired Cannon as part of its overall business strategy to become the leading global manufacturer and seller of processed foods and beverages. The business combination is expected to increase the Group's production and sales capacity in South East Asia.
Quantitative information about the expected synergies	• Goodwill arising from the business combination represents the value of Cannon's assembled workforce that is not separately identifiable and recognised, as well as future economic benefits the Group expects to realise through cost savings. The Group expects to realise recurring cost savings from implementing the Group's supply chain best practices, increased purchasing power and from optimised Group-wide support functions. The Group expects to achieve the full amount of recurring annual costs savings from 20X8 once the business of Cannon is fully integrated with the existing business operations of the Group. The Group estimates the present value of expected cost savings to be approximately CU250 million and estimates the cost to achieve these savings at approximately CU55 million.

Objectives, metrics and targets	• In line with the Group's strategy, the objectives for this business combination are:
	  • to increase the annual revenue and profit of Segment Beta by 30% and 35%, respectively, by 20X8 (compared to 20X5);
	  • to increase the Group's market share in the South East Asia by 20X8 (from approximately 15% to approximately 20%);
	  • to retain all key management personnel of Cannon; and
	  • to achieve recurring annual cost savings of approximately CU28 million for Segment Beta by 20X8 (compared to 20X5).

Objectives of the business combination

● Metrics used by management to monitor achievement of the objective

● Targets based on the metrics

The preliminary views—staff examples

Westferry's disclosure for the year ended 31 Dec 20X6 (Subsequent year)

Management's review of the performance	**Information about subsequent performance**
	• During the financial year ended 31 December 20X6, the Group's integration of Cannon continued and:
	   • revenue and profit in segment Beta increased by 20% and 25% respectively compared to the revenue and profit before the business combination;
	   • the Group increased its market share in South East Asia to 18%;
	   • the Group retained all key management personnel of Cannon as at 31 December 20X6; and
	   • the Group realised recurring annual cost savings of CU15 million for Segment Beta in 20X6, bringing the total cumulative amount of recurring annual cost savings realised since the acquisition date to CU20 million.
	
	• Management expect the Group to achieve all key objectives for the business combination, except for annual cost savings, which management now expect to achieve from 20X9.

● Metrics used by management to monitor achievement of the objective ● Actual performance in subsequent years

Feedback

Overall message

Many respondents, including almost all users, agreed with the preliminary views. However, many respondents, including almost all preparers, disagreed. Respondents identified practical challenges with the preliminary views.

Summary of feedback

- Most preparers disagreed with the preliminary views because they expect the **costs of the disclosures to outweigh the benefits:**
  - **Monetary costs:** for example, costs of collecting and auditing the information; and
  - **Proprietary costs:** for example from disclosing information some consider to be commercially sensitive and potential litigation from disclosing information some consider to be forward-looking.
- Some respondents, mainly in Europe, were also concerned that the required disclosure will put entities applying IFRS Standards at a disadvantage compared to other entities, notably those applying US GAAP.
- Many respondents said information about the performance of business combinations should be provided in **management commentary rather than financial statements.**

Practical concerns

Summary of feedback

Preparers responding to the Discussion Paper identified four practical concerns about disclosing the information described on slide 11. Our subsequent research confirmed these concerns. The concerns are:

- **commercial sensitivity**—that information could contain sensitive information that, if disclosed, could harm the entity. Respondents who disagreed said commercial sensitivity is the main practical barrier to disclosing the information identified in the preliminary views. Information most likely to be commercially sensitive is quantitative information about management's targets;
- **forward-looking information**—that information could contain information about the future that, if disclosed, could increase litigation risk. Also in some jurisdictions, providing such information in the financial statements would not allow entities to benefit from 'safe harbour' protections;
- **integration**—an entity may not be able to disclose information that is representative of the performance of a business combination if the acquired business is integrated into the entity's existing operations; and
- **auditability**—some information that would be required by the preliminary views may be costly, or difficult, to audit.

Other feedback

The management approach

Feedback summary:

- Most respondents agreed with the use of a management approach. They said it would reduce the cost of implementing the preliminary views, although some said that the management approach would still not reduce the costs sufficiently.
- However, a few respondents disagreed.

Is the CODM the right level of management?

- The IASB received mixed feedback:
  - many respondents said using the CODM to identify business combinations for which to disclose information is a practical approach that provides a reasonable cost-benefit balance.
  - many respondents said using the CODM in this way might result either in users not receiving all material information or that the CODM reviews all business combinations and therefore would not be a filter.

Location of the information

Respondents who agreed said:

- The IASB should require this information in financial statements because the IASB has **no ability** to require the information to be provided in management commentary and requiring this information in **one location** is helpful for users.

Respondents who disagreed said:

- Information about management's strategy, targets and the progress in meeting those targets should be located in management commentary for three reasons:
  - **conceptual reasons**;
  - **practical reasons** —placing information in management commentary would: (i) enable entities to benefit from 'safe-harbour' protections from potential litigation and (ii) help resolve concerns about the auditability of management's targets; and
  - to **avoid duplication** of information.

Response to feedback

Location of information	• In October 2021 the IASB tentatively decided that, based on the *Conceptual Framework for Financial Reporting*, information can be required in financial statements about the benefits an entity's management expects from a business combination and the extent to which management's objectives are being met. • However, in October 2021 the IASB also acknowledged that there may be practical reasons for not proceeding with some or all of the preliminary views.
Practical concerns	• In Q4 2021 and Q1 2022 we tested staff examples illustrating the information an entity would disclose applying the preliminary views. Staff tested the examples with various stakeholders, including members of the IASB's consultative groups. • The IASB discussed various alternatives to its preliminary views that may help better balance the cost and benefits and result in the IASB proceeding with an amended version of its preliminary views.

Possible alternatives to address practical concerns

In April 2022 the IASB discussed two variables that can be adjusted to better balance the costs and benefits of any proposed requirements:

- the **population** of business combinations for which information would be disclosed; or
- the **amount** of information to be disclosed for each affected business combination.

Population of business combinations

- Require disclosure about the strategic rationale, management objectives and subsequent performance of business combinations and expected synergies for **only a subset of 'material' business combinations**.

Amount of information

- Requiring only qualitative information in the year of acquisition rather than quantitative information.
- Specifying the metrics an entity would disclose.
- **Exempt entities from disclosing particular information in specific circumstances.**

The IASB could combine some of the alternatives, for example by requiring disclosure of information provided applying the IASB's preliminary views for a subset of business combinations but allow entities to apply an exemption in specific circumstances.

IASB tentative decision

In September 2022 the IASB tentatively decided to:

- require some of the information for **only a subset of business combinations**; and
- **exempt** entities from disclosing some information **in specific circumstances**.

The table below shows the specific pieces of information that each of these would apply to. Slides 21–22 discuss how the IASB could identify a subset of business combinations and define an exemption.

Item of Information	Continue with this preliminary view?	Require information for only a subset?	Exempt entities from disclosing information about?
Disclosure objectives	✓	N/A	N/A
Subsequent performance information:			
• Strategic rationale	✓	✗	✗
• Objective	✓	✓	✓
• Metric	✓	✓	✓
• Target	✓	✓	✓
• Actual performance in subsequent years	✓	✓	✗
Quantitative information about expected synergies in year of acquisition	✓	✗	✓

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IASB tentative decision

In September 2022 the IASB tentatively decided not to consider further an approach that would require an entity to disclose information about **specific metrics** or to disclose **no quantitative information in year of acquisition**.

Reasons for not taking forward

Specific metrics

- Feedback to the Discussion Paper indicates that using a management approach could provide more useful information.
- It could be more costly to comply with.
- It did not get significant support from consultative groups.

Only qualitative information in year of acquisition

- Although some support from consultative groups, this alternative gives a blanket exemption to all entities.
- Users would get more useful information if information requested but exemption given for specific information.

A subset of 'material' business combinations

The IASB tentatively decided to require disclosure about the objectives, metrics, targets and actual performance of business combinations for only a subset of business combinations.

A subset would be intended to capture strategically important business combinations (that is a business combination, which if it fails to achieve its objective(s) would seriously jeopardise the entity's achievement of its strategy).

Closed lists of thresholds

A subset of material business combinations would be identified using a short, exhaustive list of qualitative and quantitative thresholds. If a business combination meets any of those thresholds an entity would disclose information.

quantitative thresholds—business combinations in which the acquired business represents more than 10% of the reporting entity's revenue, operating profit or total assets.

a qualitative threshold—business combinations that aim to enter a new geographic location or start a new line of business.

This could reduce the cost of complying

Feedback received in developing the disclosure preliminary views and on the management approach in slide 16 suggests the IASB should reduce the cost of complying by reducing the number of business combinations for which information would be required.

By focusing on a subset of business combinations, users would receive the most important information about the most important business combination. Preparers would not be required to disclose information for a large number of business combinations.

Drafting an exemption

The IASB tentatively decided to exempt an entity from disclosing, in specific circumstances, information about the objectives, metrics and targets for a business combination and quantitative information about expected synergies.

How would the circumstances be identified?	The exemption is expected to be tied to the achievement of an entity's objectives. For example, allowing entities to not disclose an item of information if doing so can be expected to prejudice seriously any of the entity's key objectives for the business combination.
What practical concerns would an exemption resolve?	• **Commercial sensitivity** The exemption based on prejudicing an entity's objective(s) for a business combination should capture commercial harm from a range of sources—for example competitors using the information or litigation by users or other parties. • **Some elements of litigation risk** For example, if the risk arises because an entity failed to meet an objective as a result of the disclosure. Litigation arising for other reasons would not be covered.
What application guidance would be included?	• Requirements—for example disclosing the reason for applying the exemption separately for each item of information. • Considerations of when it is appropriate to use the exemption—for example, it would be inappropriate if that information was already disclosed elsewhere.

Contribution of the acquired business

The IASB's preliminary view is that it should retain the requirement for information to be disclosed for the combined entity as if the BC had occurred at the start of the reporting period, but:

a) replace the term 'profit or loss' in paragraph B64(q) of IFRS 3 with the term 'operating profit before deducting acquisition-related costs and integration costs'. Operating profit or loss would be defined as in the Exposure Draft *General Presentation and Disclosures*; and

b) add to paragraph B64(q) a requirement to disclose cash flows from operating activities.

Summary of feedback

There was mixed feedback on the IASB's preliminary views. In particular, many respondents disagreed with the IASB's preliminary view that it should require disclosure of operating cash flow information.

Tentative decisions (November 2021)

- Retain the requirement in paragraph B64(q).
- Explain the objective of the requirement but not provide guidance on how to prepare the information.
- Specify that the basis that an entity applies in preparing the information required by paragraph B64(q) is an accounting policy.
- Replace the term 'profit or loss' in paragraph B64(q) with 'operating profit or loss'. 'Operating profit or loss' will be as defined in the IASB's Primary Financial Statements project.
- Not add a requirement to disclose information about cash flows arising from operating activities.

Liabilities arising from financing activities and defined benefit pension liabilities

The IASB's preliminary view is that it should specify that financing and pension liabilities are major classes of liabilities. As a result, an entity would be required to disclose the amount of such liabilities acquired for each business combination (if the information is material).

Summary of feedback

Most respondents commented **agreed.**

Tentative decisions (November 2021)

- The IASB tentatively decided to achieve the objective of its preliminary view by not specifying that these liabilities are major classes of liabilities but instead by proposing to amend:
  - paragraph B64(i) of IFRS 3* to remove the term 'major'; and
  - paragraph IE72 of the Illustrative Examples accompanying IFRS 3 (which illustrates the application of paragraph B64(i)) to illustrate liabilities arising from financing activities and defined benefit pension liabilities as classes of liabilities assumed.

*B64(i) of IFRS 3 requires the entity to disclose the amounts recognised as of the acquisition date for each major class of assets acquired and liabilities assumed.

Questions?

❷ Should amortisation of goodwill be reintroduced?

The preliminary view

Reintroducing amortisation

- Retain the impairment-only approach (small majority).
- The IASB welcomed feedback that provides new practical or conceptual arguments, together with evidence for these arguments.

Convergence with US GAAP

- The IASB asked stakeholders whether their views depend on whether the outcome would be consistent with US Generally Accepted Accounting Principles (US GAAP).

Feedback

Overall message

Respondents' views remain mixed. Many respondents agreed with the preliminary view to retain the impairment-only model but many disagreed, saying amortisation of goodwill should be reintroduced.

Summary of feedback

- Respondents generally **did not provide new conceptual arguments or evidence**, although some respondents considered that there is new practical evidence since IFRS 3 was issued in 2004 being that the impairment test is not effective enough. Respondents referred to the evidence from applying the impairment-only model since 2004 and the problems encountered as new evidence.
- Most respondents who commented said **convergence with US GAAP** was desirable. However, many respondents also said their view did not depend on whether the outcome would maintain convergence, or that the IASB should make its decision based on evidence it has collected rather than solely to maintain convergence.

Feedback

Reasons for reintroducing amortisation	Reasons for retaining impairment-only approach
Conceptual reasons • Goodwill is a wasting asset and amortisation of goodwill would reflect its consumption. • Amortisation prevents the recognition of internally generated goodwill. • A reliable estimate of useful life can be made. • Amortisation helps hold management accountable. **Practical reasons** • The impairment test is not working. • Goodwill balances are too high. • Reintroducing amortisation would resolve concerns that entities do not recognise impairment losses on a timely basis. • Amortisation is a simple method that would reduce costs. • Earnings would be less volatile, helping financial stability.	**Conceptual reasons** • Goodwill is not a wasting asset with a determinable useful life. • Impairment losses provide users with more useful information than amortisation. • The useful life of goodwill cannot be estimated reliably. • The impairment-only model helps hold management accountable better than an amortisation model. **Practical reasons** • Reintroducing amortisation would not resolve concerns that entities do not recognise impairment losses on a timely basis. • Compelling evidence for change has not been identified.

Staff observations

Impairment-only vs amortisation	• There remain **divergent and strongly held** views on whether to retain the impairment-only model or reintroduce an amortisation model. The arguments provided to support either approach are often **diametrically opposed** (see slide 29). In addition many of the arguments provided had been made during the development of IFRS 3 or during the course of this project. • There appears to have been a **shift** in the balance of user views since the PIR of IFRS 3 with more users supporting the reintroduction of amortisation. However user views remain **mixed**.
Amortisation model	• When the IASB decided to adopt the impairment-only model, not being able to reliably estimate the useful life of goodwill was central to its conclusions. Some respondents to the Discussion Paper however said a reliable estimate can be made. • A few respondents were concerned about the consequences of transitioning to an amortisation-based model, for example on entities' financial positions and stability.
Convergence with US GAAP	• The importance of convergence (and maintaining convergence) is evident from the feedback. Additionally, IOSCO made a public statement shortly after the comment letter period had closed **encouraging the IASB and the FASB to work collaboratively** on this matter.

Further research

In September 2021, the IASB asked us to further analyse two specific aspects of feedback on whether the IASB should reintroduce amortisation of goodwill including:

	Useful life of goodwill	Transition
Focus of our research	• Whether it is feasible to estimate a useful life of goodwill and the pattern in which it diminishes, that faithfully represents its decline in value.	• The potential consequences of transitioning to an amortisation-based model were the IASB to reintroduce amortisation of goodwill.
Process	• Discussed this topic at the November 2021 Capital Markets Advisory Committee (CMAC) and Global Preparers Forum (GPF) meetings. We held one-to-one meetings with preparers, preparer groups, auditors and users. We also sent an information request to national standard-setters.	• Discussed the issue at the November 2021 GPF meeting. We sent an information request to national standard-setters and regulators.

The IASB has not decided whether to retain the impairment-only model or whether to explore reintroducing amortisation of goodwill, but further information on these two topics will help the IASB in making that decision, planned for Q4 2022.

Research—estimating the useful life of goodwill

Feasibility	• There are several factors and methods entities would use to estimate the useful life of goodwill. For some entities, making this estimate would be relatively straightforward given the finite nature of the businesses they acquire. For other entities, making this estimate would be more subjective and entities may need to consider several factors or use proxies. • This diversity of factors and methods might be a result of different facts and circumstances of each business combination, different judgements of what goodwill is or different preferences in the method(s) selected. • Many preparers suggested specifying an upper limit for practical reasons or to prevent excessively long useful lives being used. • Many preparers expressing a view said the pattern goodwill diminishes should not necessarily be straight-line but many said a straight-line approach should be adopted as a practical solution.
Auditability	• Auditors said it would be possible to audit managements' estimates of useful life, but most of them suggested providing application guidance, for example, on unit of account, when to use particular factors and so on.
Usefulness	• Users had mixed views. Many said a useful life and amortisation pattern based on management's estimate would provide useful information, for example it would provide insight into management's assessment of the recovery period for the investment and the rationale for the purchase price. • However, many said an amortisation charge would be arbitrary due to the difficulty of estimating the useful life of goodwill and would not provide useful information.

Research—potential consequences of transition

Feedback

- Most respondents highlighted potential consequences of transitioning to an amortisation-based model and many respondents said transition would significantly affect entities' financial positions and performance because of the size of historic goodwill balances.
- Some of these effects could be significant and more prevalent for entities in particular jurisdictions:
  a) respondents from Asia-Oceania said entities in their jurisdictions risk failing to meet listing requirements and, eventually, being suspended from trading or delisted if they report negative equity and/or profit; and
  b) respondents from Latin America said the amounts of dividends entities in their jurisdictions could distribute would be affected.
- However, many other respondents said the consequences would be limited. Some said the consequences are not compelling enough to prevent reintroducing amortisation of goodwill.

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❸ Other topics

Effectiveness of the impairment test

Preliminary view	It is not feasible to design a different impairment test for cash-generating units (CGUs) containing goodwill that is significantly more effective at recognising impairment losses on goodwill on a timely basis than the impairment test set out in IAS 36 *Impairment of Assets*.
Overall message	Most respondents agreed with the preliminary view. However, many respondents suggested ways to **improve the application** of the impairment test in IAS 36.

Summary of feedback

Respondents who agreed said:

- the 'headroom approach' would increase costs and complexity for preparers but would only reduce shielding rather than eliminating it.
- many of these respondents also said that, for this reason, the IASB should reintroduce amortisation.
- the test is wrongly considered not robust enough because the purpose of the impairment test is misunderstood and it is unrealistic to expect impairment losses to be recognised without delay.

Respondents who disagreed said:

- there are ways to improve the impairment test, including the headroom approach, other approaches or a full review of IAS 36.
- it is possible to make some targeted improvements to the impairment test in IAS 36—for example disclosures to combat management over-optimism and ways to improve the level at which goodwill is allocated to CGUs.

Simplifying the impairment test

Preliminary views	• Remove the requirement to perform the quantitative impairment test annually. • Simplify how an entity calculates value in use through changes to the discount rate used and the inclusion of some cash flows related to restructuring.
Overall message	**Most respondents**, including some preparers, **did not support** the IASB's preliminary view that it should provide relief from the annual quantitative impairment test of CGUs containing goodwill. **Respondents generally welcomed** the IASB's preliminary views on simplifying and improving how to estimate **value in use** (VIU).

Summary of feedback

- Most respondents disagreed with removing the requirement for a mandatory annual quantitative impairment test of CGUs containing goodwill. Many of them expressed concern that any cost savings would not outweigh the resulting reduction of the effectiveness and robustness of the test. Some of these respondents said if amortisation was reintroduced, they could accept simplifying the impairment test.

- Many respondents agreed that the IASB should (a) allow an entity to use post-tax cash flows and post-tax discount rates in estimating VIU; and (b) remove from IAS 36 restrictions on including in estimates of VIU cash flows arising from a future restructuring to which an entity is not yet committed or from improving or enhancing an asset's performance.

Intangible assets acquired in a business combination

Preliminary views	Not to change the recognition criteria for identifiable intangible assets acquired in a business combination.
Overall message	**Most** respondents **agreed**.

Summary of feedback

- Most respondents, including many users, agreed with the preliminary view. In their view, goodwill and other intangible assets acquired in a business combination are different in nature and recognising these assets separately provides users with better and more useful information.
- However, a few of these respondents said if the IASB reintroduces amortisation of goodwill, it should also, on cost-benefit grounds, consider including some identifiable intangible assets acquired in a business combination in goodwill. In these respondents’ view, if the same subsequent accounting approach is applied to both goodwill and these intangible assets, it would no longer be necessary to recognise those intangible assets separately.
- Some respondents, including some users, disagreed with the preliminary view for various reasons. In their view, **separately recognising acquired intangible assets does not provide useful information** and the costs of doing so outweigh the benefits.

Total equity excluding goodwill

Preliminary views	Require an entity to present the amount of total equity excluding goodwill.
Overall message	**Almost all** respondents who commented disagreed.

Summary of feedback

- Almost all respondents who commented on this issue disagreed with the preliminary view. In their view, the presentation is unnecessary and lacks conceptual basis. Most of these respondents also said users could easily compute total equity excluding goodwill based on information already in financial statements.
- A few respondents agreed with the preliminary view. These respondents said presenting the amount on the statement of financial position would bring greater transparency to financial statements and help highlight risky businesses to users, especially to relatively inexperienced users.

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Questions?

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