IFRS

STAFF PAPER

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IASB® Meeting

Project	**Goodwill and Impairment research project**		
Paper topic	Next stage in the research project		

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Purpose

1. The purpose of this paper is for the Board to decide whether the next stage in the Goodwill and Impairment research project (the research project) is to issue a Discussion Paper or an Exposure Draft.

Structure of the paper

2. The paper is structured as follows:

   (a) background and introduction (paragraphs 3–11)

   (b) summary of due process requirements (paragraphs 12–17)

   (c) staff analysis (paragraphs 18–69)

   (d) staff conclusions (paragraphs 70–77)

   (e) staff recommendation (paragraphs 78–79)

   (f) question for the Board

   (g) Appendix A—Background on the PIR of IFRS 3 *Business Combinations*

   (h) Appendix B—The Board's tentative decisions so far

   (i) Appendix C—Factors to consider in determining whether a Discussion Paper or an Exposure Draft is appropriate

Background and introduction

3. The Board added the research project to its agenda as a follow-up of its Post-implementation Review (PIR) of IFRS 3. See *Appendix A* for further background on the PIR.

4. Of the topics on which the Board sought feedback during the PIR, the Board identified the following topics for further research and follow-up:

   (a) the recognition of intangible assets separately from goodwill;

   (b) impairment of goodwill and indefinite-lived intangible assets; and

   (c) disclosures.

5. In adding those topics to its research agenda, the Board observed that:

   (a) the feedback from the PIR of IFRS 3 did not highlight areas where unexpected costs or implementation problems were encountered, and consequently, did not highlight an immediate need to amend IFRS 3, IAS 36 *Impairment of Assets* or IAS 38 *Intangible Assets*;

   (b) some of the topics identified for further follow-up were contentious during the development of IFRS 3 and the feedback from the PIR did not provide new information to the Board;

   (c) more research was required:

      (i) to understand the reasons for stakeholders' concerns, especially whether the concerns arose because of problems or shortcomings with the existing requirements; and

      (ii) to assess if there are ways of resolving those problems.

6. On the basis of stakeholders' feedback received during and after the PIR of IFRS 3, the Board set the research project the objective of investigating the following four questions:

   (a) are there new conceptual arguments or new information to support reintroducing amortisation of goodwill?

   (b) could some identifiable intangible assets acquired in a business combination be allowed to be included within goodwill without losing the information currently provided to users of financial statements?

(c) can better and more timely information about goodwill and impairment be provided to users of financial statements without imposing costs on preparers that exceed the benefits?

(d) can the application of the requirements in IAS 36 be improved by:

(i) simplifying the test without making it less robust; and/or

(ii) making the test more effective at timely recognition of impairments of goodwill?

7. The Board observed that the objectives are interconnected, as are possible approaches for achieving the objectives. For example, simplifying the impairment test makes it more difficult to improve the effectiveness of the impairment test and vice versa. Similarly, reintroducing amortisation of goodwill might eliminate or reduce concerns about the effectiveness of the impairment testing of goodwill, and might remove one obstacle to allowing some identifiable intangible assets with a finite life to be included within goodwill acquired in a business combination. Consequently, the Board concluded that it should:

(a) assess whether and how a possible approach to achieving each specified objective contributes to achieving other objectives; and

(b) identify a balanced package of possible approaches in response to stakeholder feedback during and after the PIR.

8. So far, the Board has discussed:

(a) whether there are new conceptual arguments, or new information, to support reintroducing amortisation of goodwill;

(b) possible ways of improving the application of the requirements in IAS 36; and

(c) possible improvements to the disclosure requirements about goodwill and impairment.

See paragraph B1 of *Appendix B* for a summary of the possible approaches discussed by the Board.

9. At its December 2017 and January 2018 meetings the Board tentatively decided:

(a) not to consider reintroducing amortisation of goodwill.

(b) to consider improving the application of IAS 36 by:

 (i) making impairment testing of goodwill more effective by using the unrecognised headroom of a cash-generating unit (or groups of units) as an additional input in the impairment testing of goodwill. Unrecognised headroom is the excess of the recoverable amount of a unit (or groups of units) over its carrying amount.

 (ii) amending the calculation of value in use of an asset (or a cash-generating unit) by removing the requirement to exclude from the calculation of value in use those cash flows that would result from a future restructuring or from a future enhancement.

 (iii) removing the explicit requirement to use pre-tax inputs in calculating value in use, and to disclose pre-tax discount rates used. Instead, an entity would be required to use internally consistent assumptions about cash flows and discount rates, and to disclose the discount rate(s) actually used.

(c) to consider introducing requirements for an entity to disclose:

 (i) each year, information about the headroom in a cash-generating unit (or groups of units) to which goodwill is allocated for impairment testing.

 (ii) each year, a breakdown of goodwill by past business combination, explaining why the carrying amount of goodwill is recoverable.

 (iii) the reasons for paying a premium that exceeds the value of the net identifiable assets acquired in a business combination, key assumptions or targets supporting the purchase consideration and, then subsequently each year, a comparison of actual performance with those assumptions or targets.

See paragraph B2 of *Appendix B* for the staff's assessment of the extent to which the changes listed above would help in providing satisfactory answers to the four questions investigated in the research project.

10. At the April 2018 meeting, the Board is considering whether some identifiable intangible assets acquired in a business combination could be allowed to be included within acquired goodwill. (See Agenda Paper 18A.)

11. This paper assumes that the Board would decide to consider allowing some identifiable intangible assets acquired in a business combination to be included within goodwill.

Summary of due process requirements

12. In deciding whether the next stage of the research project is to issue a Discussion Paper or an Exposure Draft, the Board is guided by the requirements in the IFRS Foundation *Due Process Handbook*.

13. Paragraph 4.12 of the *Due Process Handbook* states that the main output of the research programme is expected to be Discussion Papers and research papers. Discussion Papers are designed to elicit comments from interested parties that can help the Board decide whether to add a project to its standard-setting programme. In other words, a Discussion Paper helps the Board in seeking feedback on whether the evidence gathered in a research project supports a standard-setting action by the Board. A Discussion Paper typically includes a comprehensive overview of the issue, possible approaches to addressing the issue, the preliminary views of the Board and an invitation to comment.

14. However, paragraph 5.5 of the *Due Process Handbook* states that the Board is not required to publish a Discussion Paper before adding a standard-setting project to its agenda if the Board is satisfied that it has sufficient information and understands the problem and the potential solutions well enough to proceed without a Discussion Paper. The Board might conclude that a Discussion Paper is not necessary because it has sufficient input from its research project to proceed directly to an Exposure Draft. The Board is required to report to the Due Process Oversight Committee the reasons for not publishing a Discussion Paper.

15. Paragraph 5.4 of the *Due Process Handbook* states that, in adding a standard-setting project, the Board evaluates the merits of adding the project primarily on the basis of the needs of users of financial reports. The Board also

takes into account the costs of preparing the information in financial reports. When deciding whether a proposed agenda item will address users' needs, the Board considers:

(a) whether there is a deficiency in the way particular types of transactions or activities are reported in financial reports;

(b) the importance of the matter to those who use financial reports;

(c) the types of entities likely to be affected by any proposals, including whether the matter is more prevalent in some jurisdictions than others; and

(d) how pervasive or acute a particular financial reporting issue is likely to be for entities.

16. Before adding a standard-setting project, the Board is required to consult its advisory bodies—the IFRS Advisory Council and the Accounting Standards Advisory Forum (paragraph 5.6 of the *Due Process Handbook*).

17. Board members may find it helpful to refer to paragraphs 24–41 of Agenda Paper 28 for the February 2018 Board meeting when considering the staff analysis in this paper. Those paragraphs have been reproduced in *Appendix C* and renumbered for convenience of referring to those paragraphs in the staff analysis below.

Staff analysis

18. Issuing a Discussion Paper, and reviewing the feedback received on it, would be the expected outcome at the end of the research project as specified in the *Due Process Handbook* (see paragraph 13).

19. However, the Board could consider issuing an Exposure Draft provided it is satisfied that there is sufficient evidence to proceed with standard-setting. Paragraphs 20–69 contain the analysis of whether there is sufficient evidence to proceed with standard-setting on the Board's tentative decisions. Sufficiency of evidence has been assessed by analysing the factors set out in paragraph 5.4 of the *Due Process Handbook* (see paragraph 15). That analysis is divided into the following sections:

(a) headroom approach (paragraphs 20–39);

(b) calculating value in use—removing restriction that excludes specified cash flows (paragraphs 40–50);

(c) possible additional disclosure requirements (paragraphs 51–56); and

(d) intangible assets acquired in a business combination (paragraphs 57–61); and

(e) calculating value in use—using internally consistent pre-tax or post-tax inputs (paragraphs 62–69).

Headroom approach

Would the approach produce benefits for users?

20. Investors have consistently stated that recognising impairment losses in an entity's financial statements provides targeted useful information that confirms, and never precedes, investors' assessments and consideration of those losses, and that helps investors assess management's stewardship. For these reasons, although there were concerns that the delay between the events triggering impairment and the recognition of impairment loss in the entity's financial statements was generally unacceptably long, some investors have never asked the Board to resolve that problem. However, some investors have asked the Board to improve the timing of recognition of impairments of goodwill.

21. Other stakeholders, such as national standard-setters and regulators, also have asked the Board to resolve or reduce the problem of delayed recognition of impairment losses.

22. The Board analysed the issue and observed that acquired goodwill is shielded from impairment by the unrecognised headroom in the unit. The unrecognised headroom is the excess of the recoverable amount of the unit over its carrying amount; it comprises internally-generated goodwill, any unrecognised intangible assets and the difference between current value and carrying amount of net assets not measured at current value. The shielding effect arises because the unrecognised headroom absorbs the entire first layer of year-on-year decreases in total headroom (sum of unrecognised headroom and acquired goodwill). An

impairment loss on acquired goodwill is recognised only when a decrease in a unit's total headroom eliminates its unrecognised headroom.

23. The Board also observed that, in situations in which an acquired business is merged into an existing unit (or groups of units) with significant unrecognised headroom and acquired goodwill is tested for impairment at the level of that unit (or groups of units), the current impairment test does not provide information about the success or failure of the business combination. This is because the current impairment test results in recognition of an impairment loss on goodwill only when there are events that negatively affect the unit (or groups of units) as a whole, and not just the acquired business, so significantly that they wipe out all of the unrecognised headroom. This inevitable consequence of the current impairment test possibly explains, at least partly, feedback from investors that there is insufficient information in the financial statements to assess the success or failure of a business combination.

24. The fact that internally-generated goodwill has a shielding effect for acquired goodwill is not new information for the Board. When revising IAS 36 in 2004 to remove amortisation of goodwill, the Board concluded that acquired goodwill will always be shielded from impairment by internally-generated goodwill because it is not possible to measure separately goodwill generated internally after a business combination and to factor that measure into the impairment test. Therefore, the Board took the view that the objective of the goodwill impairment test could at best be to ensure that the carrying amount of goodwill is recoverable from future cash flows expected to be generated by both acquired goodwill and goodwill generated internally after the business combination. (See paragraph BC135 of the Basis for Conclusions on IAS 36.)

25. To respond to the feedback received in the PIR, the Board developed the headroom approach as a way to provide more timely recognition of impairment loss for goodwill by removing the shielding effect of the unrecognised headroom. See Agenda Paper 18C for the December 2017 Board meeting for a detailed analysis of the headroom approach. Alternatively, see pages 10–19 of ASAF Agenda Paper 5 of the April 2018 meeting of the Accounting Standards Advisory Forum for a crisp description of the approach.

26. Applying the headroom approach, an entity compares the total headroom at the current impairment testing date with the total headroom at the immediately preceding impairment testing date. Any decrease in total headroom is presumed to relate only to acquired goodwill and is recognised as an impairment loss. However, an entity could rebut the presumption if there is evidence that all or part of the decrease instead relates to unrecognised headroom. The Board also considered requiring the entity to explain in its financial statements the basis of attribution of any decrease in total headroom.

27. The headroom approach would be likely to bring in more discipline in impairment testing of goodwill because:

    (a) in applying the rebuttable presumption, an entity would need to think carefully about factors affecting acquired goodwill.

    (b) management of the entity would be discouraged from making over-optimistic projections of cash flows because any difficulty in maintaining the over-optimism year after year reduces the total headroom, potentially resulting in the recognition of an impairment loss on acquired goodwill.

28. Investors are likely to benefit from the disclosure of basis used for attributing the decrease in total headroom. This information is not available to investors in the current impairment test.

29. The staff consulted the Capital Markets Advisory Committee (CMAC) on the headroom approach. See Agenda Paper 18C for the detailed meeting notes of the CMAC meeting.

30. A majority of CMAC members supported the headroom approach because it would remove the shielding effect of any unrecognised headroom. Some members supported the Board's idea of requiring disclosure of the basis of attributing the decrease in total headroom. Those members thought that such disclosure would provide useful information to investors. Some members indicated a preference for disclosure of headroom instead of using the headroom approach for impairment testing. However, those members thought that companies are likely to apply a disclosure-only requirement less rigorously than if they have to use the headroom for impairment testing purposes.

31. One member cautioned that using a rebuttable presumption could lead to decreases in total headroom being attributed to acquired goodwill even if the decrease was caused by reasons not connected to the acquired goodwill. This is likely to happen if an entity chooses to attribute all of the decrease in total headroom to acquired goodwill and to recognise an impairment loss without assessing the reasons for the decrease. The member stated that such information is not useful to investors.

32. On the basis of the analysis in paragraphs 20–31, there is evidence that the headroom approach would produce benefits for users of financial statements by providing information that is relevant and currently not available to them, and by providing more timely information about impairment of goodwill.

Costs of applying the headroom approach

33. When developing the headroom approach, the Board considered whether the headroom approach would significantly increase the cost and complexity of impairment testing of goodwill. The Board observed that the approach does not add complexity to the impairment test because it just adds one more input to the existing calculations. Information about unrecognised headroom or total headroom is generally available from the current impairment testing model for goodwill because recoverable amount is calculated annually for testing goodwill for any impairment. However, an entity may have to perform some specified additional tasks to apply the headroom approach, which would add to the cost of impairment testing (see paragraph 37).

34. The staff consulted the Global Preparers Forum (GPF) to understand the nature and extent of costs that are likely to be incurred in applying the headroom approach. The feedback of GPF about costs was consistent with the costs identified by the Board. See Agenda Paper 18C for the detailed meeting notes of the GPF meeting.

35. Most GPF members said that the headroom approach is likely to add significant costs to the impairment testing of goodwill, for two reasons.

    (a) currently, companies generally do not perform a detailed calculation of recoverable amount if, on the basis of estimates, averages and computational short cuts, it is clear that the recoverable amount would be sufficiently higher than the carrying amount of the cash generating unit (or groups of units). However, to use the headroom approach, a more precise measurement of recoverable amount would be required every year.

(b) rebutting the presumption would cause significant incremental debate with auditors and would also attract questions from regulators.

36. Some members said that there would be costs involved in tracking actual performance against the assumptions made in analysing the factors that support the consideration paid for the business combination.

37. The Board identified some additional tasks needed to apply the headroom approach in full, which would add to the cost of impairment testing. In the following events, an entity would have to carry out additional one-time tasks for calculating the unrecognised headroom:

(a) for an existing unit that does not contain goodwill and to which newly acquired goodwill has been allocated for the first time, the entity would need to determine the recoverable amount of the existing unit just before the business combination—the pre-combination unrecognised headroom would be used as an input when performing impairment testing of goodwill of the unit for the first time after the business combination.

(b) for a unit that is partially disposed of (and for which not all previously acquired goodwill is derecognised), the entity would need to determine the recoverable amount of the unit immediately after the disposal—the post-disposal unrecognised headroom would be used as an input at the next impairment testing.

(c) for a restructured unit, the entity would need to determine the recoverable of the unit immediately after the restructuring—the post-restructuring unrecognised headroom would be used as an input at the next impairment testing.

38. Having identified these additional tasks, the Board thought that it could decide not to require these additional tasks, on cost-benefit grounds, in which case the headroom approach would not be available for that unit in that period. The

recoverable amount calculations at the first impairment testing date after the event provide the headroom information for the subsequent impairment testing.

39. Although benefits and costs of the headroom approach have been identified, more work is required to understand the extent of costs that are likely to be incurred in applying the headroom approach and conclude that the expected benefits exceed the cost of applying the approach. This would involve extensive outreach:

   (a) with investors to explain the information produced by applying the headroom approach; and

   (b) with preparers to better understand whether and when recoverable amount of a unit (or groups of units) is determined annually with precision.

Calculating value in use
Removing restriction that excludes specified cash flows

40. The Board tentatively decided to consider removing the requirement for an entity to exclude from the calculation of value in use those cash flows that would result from a future restructuring or from a future enhancement. See Agenda Paper 18B for the January 2018 Board meeting for a detailed analysis of the issue and the arguments in support of the Board's tentative decision.

41. The Board thought that removing that requirement would eliminate an inconsistency in IAS 36, by:

   (a) capturing within value in use the cash flows that result from an existing potential to restructure or enhance an existing asset, as is also the case for fair value;

   (b) adopting the same unit of account for value in use as is done for fair value less costs of disposal;

   (c) avoiding applying to the determination of value in use a liability recognition criterion that is not pertinent to the measurement of an asset; and

   (d) avoiding applying a rule that excludes some cash flows to avoid unjustifiably optimistic assumptions, but that is inconsistent with the underlying concepts and would be more appropriately addressed by auditors or enforcers.

Would the change produce benefits for users?

42. The request for the Board to consider removing the restriction that excludes cash flows from future restructuring and from future performance enhancements was mainly from preparers. The staff outreach with investors so far has focussed on effectiveness of impairment testing of goodwill and information needs of investors in relation to business combinations.

43. Having said that, investors are likely to benefit from the information produced by removing that exclusion mainly for the reasons explained in paragraphs 41(a) and 41(b). See paragraphs 11–15 of Agenda Paper 18B for the January 2018 Board meeting. Some investors are likely to support removing that exclusion for a simple reason that the resulting information gives them an insight into what management expects will happen in future.

44. Some investors may not support removing that exclusion because of concerns about the entity-specific nature of value in use and, consequently, the scope it arguably provides management to include unjustifiably optimistic inputs to pass the impairment test.

45. On the basis of the analysis in paragraphs 42–44, it is not clear whether removing the restriction that excludes cash flows from future restructuring and from future performance enhancements in calculating value in use would, on balance, produce net benefits for investors.

Costs of preparing the information

46. IAS 36 anchors the estimates of future cash flows in management's budgets and forecast. The IAS 36 restriction on the cash flows means that the budgeted or forecast cash flows need to be split into two components, for example to separate forecast capital expenditures between maintenance capital expenditures and expansionary capital expenditures. Removing that restriction would appear to eliminate unnecessary costs and complexity for preparers.

47. However, the Board observed that it may be difficult in practice to distinguish between an existing potential, already contained within an asset, to enhance that

asset, and the possible future acquisition of a different asset. This difficulty is exacerbated because management's budgets/forecasts may tend to be set at a level that is challenging, rather than at a level that provides a realistic prediction of what will ultimately happen.

48. Furthermore, to reflect the value of a potential that exists in an asset at the measurement date, an entity might have to use expected value techniques. For example, if the restructuring or enhancement is not certain to occur, the fair value would reflect the probability of its occurrence, and would not assume that the restructuring or enhancement is certain. Similar techniques might be considered appropriate in estimating value in use, if the restriction were to be removed.

49. Preparers are likely to argue that budgets/forecasts that are the basis for cash flow projections will reflect a single estimate of future cash flows. Using expected value techniques would be likely to increase the costs of impairment testing.

50. On the basis of the analysis in paragraphs 46–49, it is not clear whether removing the restriction that excludes cash flows from future restructuring and from future performance enhancements in calculating value in use would eliminate unnecessary costs and complexity for preparers. However, there could possibly be some saving in costs and complexity if that exclusion is limited so that value in use includes cash flows from only those future restructuring and from future performance enhancements that the entity is more likely than not to undertake.

Possible additional disclosure requirements

51. In response to feedback and suggestions from investors during and after the PIR, the Board tentatively decided to consider introducing requirements for an entity to disclose:

    (a) each year, information about the headroom in a cash-generating unit (or groups of units) to which goodwill is allocated for impairment testing.

    (b) each year, a breakdown of goodwill by past business combination, explaining why the carrying amount of goodwill is recoverable.

    (c) the reasons for paying a premium that exceeds the value of the net identifiable assets acquired in a business combination, key assumptions or targets supporting the purchase consideration and, then subsequently each year, a comparison of actual performance with those assumptions or targets.

See Agenda Paper 18F for the December 2017 Board meeting for a detailed analysis.

52. However, if feedback from GPF is considered representative of the view of preparers generally, preparers may not be supportive of the possible disclosure requirement set out in paragraph 51(c). Many GPF members expressed concerns that for those disclosures to be meaningful an entity would have to disclose commercially sensitive information; consequently, if the Board requires those disclosures, entities are likely to disclose only boilerplate information. The feedback is likely to be the same whether the requirement would be to disclose quantitative information or qualitative information.

53. A few GPF members argued that providing the disclosures for each individual acquisition would be difficult because post-acquisition integration could make it difficult for management to track those targets or assumptions vis-à-vis actual performance.

54. Paragraphs B10–B15 of Agenda Paper 18F for the December 2017 Board meeting set out the staff thoughts on availability of information to disclose the information envisaged in paragraph 51(c).

55. There is a clear need for more outreach with preparers to understand the costs of preparing information, especially the information envisaged in paragraph 51(c). A cost-benefit analysis will not be possible without understanding better the costs of preparing that information.

56. The cost-benefit analysis of possible disclosure of headroom is likely to be similar to the cost-benefit analysis of using headroom information in impairment testing of goodwill.

Intangible assets acquired in a business combination

57. See Agenda Paper 18A for a detailed analysis of the feedback received during and after the PIR and the approaches considered by the Board to respond to the feedback.

58. Because the requirement in IFRS 3 to recognise all identifiable intangible assets acquired in a business combination separately from goodwill is converged with the equivalent requirement in US GAAP, the Board may want to consider the plan of the US Financial Accounting Standards Board (FASB).

59. The FASB has on its agenda a research project to consider one of more of the following:

    (a) reintroducing amortisation of goodwill.

    (b) subsuming certain customer related intangible assets and all non-competition agreements into goodwill and amortising goodwill.

    (c) further simplifying the impairment test by requiring testing of goodwill for any impairment:

        (i) upon a triggering event; and

        (ii) at an entity level.

60. The FASB plans to commence its discussions in the third quarter of 2018. Its decision about the form of consultation document, ie Exposure Draft or Discussion Paper, will depend on the outcome of its discussions.

61. If the Board decides to pursue allowing some indefinite-lived intangible assets acquired in a business combination to be included within goodwill, loss of information for investors would be offset to some extent by the qualitative disclosures that an entity would have to provide. However, the extent of cost savings for preparers is not clear, and consequently more work is required to assess the possible benefits of making that change—cost savings for preparers—and possible costs of that change—loss of information of users.

Calculating value in use
Using internally consistent pre-tax or post-tax inputs

62. The Board tentatively decided to:

(a) remove the explicit requirement to use pre-tax inputs in calculating value in use, and to disclose pre-tax discount rates used; and

(b) instead, require an entity to use internally consistent assumptions about cash flows and discount rates, and to disclose the discount rate(s) actually used.

63. See Agenda Paper 18A for the January 2018 Board meeting for a detailed analysis of the issue and the arguments in support of the Board's tentative decision.

Would the change produce benefits for users?

64. During and after the PIR, several stakeholders—investors, preparers, valuation experts and members of the Board's consultative groups—have said that a pre-tax discount rate is hard to understand and does not provide useful information as that rate is not observable and is generally not used for valuation purposes. Current value of an asset is regarded and understood as a post-tax measure.

65. As explained in Agenda Paper 18A for the January 2018 Board meeting, a pre-tax discount rate is not generally observable. It is generally derived by first discounting post-tax cash flows using a post-tax discount rate to determine a present value, and then using reverse engineering (back solving) to find the pre-tax discount rate that must be applied to the pre-tax cash flows to obtain the same present value. Disclosure of such computed pre-tax rate does not provide useful information because it is not the input that was used in computing the recoverable amount of an asset (or a cash-generating unit).

66. Consequently, removing the explicit requirement to use pre-tax inputs and rather requiring disclosure of discount rate(s) actually used in calculating value in use would produce information that is useful to investors.

Costs of preparing the information

67. An entity is not likely to incur any costs if the Board's tentative decision is implemented. Instead, there would be a saving in costs because the entity, if it used post-tax inputs, would no longer be required to use reverse engineering (back solving) to derive the pre-tax discount rate.

68. The Board's tentative decision would make calculating value in use applying IAS 36 consistent with the requirements in IFRS 13 *Fair Value Measurement* for

determining fair value (and hence for determining fair value less costs of disposal).[1] It would also be consistent with the removal from IAS 41 *Agriculture* of a reference to pre-tax discount rates in 2008 (see paragraphs BC5–BC6 of the Basis for Conclusions on IAS 41 [reproduced in *Appendix C* of Agenda Paper 18A for the January 2018 Board meeting]).

69. On the basis of the analysis in paragraphs 64–68, it is clear that the Board's tentative decision would produce benefits, though not substantial, without causing any costs.

Staff conclusions

70. On the basis of the analysis in paragraphs 20–69, the staff have concluded that the following changes need more outreach and analysis to understand the costs and establish that the expected benefits exceed the expected costs before the staff would recommend that the Board should proceed to standard-setting:

(a) headroom approach;

(b) removing the restriction that excludes from the calculation of value in use those cash flows that would result from a future restructuring or from a future enhancement;

(c) possible additional disclosure requirements about business combinations, goodwill and impairment; and

(d) allowing some indefinite-lived intangible assets acquired in a business combination to be included within acquired goodwill.

71. However, in relation to the Board's tentative decision to consider removing the requirement in IAS 36 to specifically use pre-tax inputs, the staff have concluded that there is sufficient evidence for the Board to proceed with proposing amendments to IAS 36.

[1] Appendix B of IFRS 13 provides application guidance on present value techniques. IFRS 13 does not specify whether an entity should use pre-tax or post-tax inputs in measuring fair value. Instead, the Standard specifies that assumptions about cash flows and discount rates should be internally consistent. After-tax cash flows should be discounted using an after-tax discount rate. Pre-tax cash flows should be discounted at a rate consistent with those cash flows. (See paragraph B14 of IFRS 13.)

72. In relation to the Board's tentative decisions identified in paragraph 70 as needing more work, the Board could either:

(a) continue to gather more evidence through field testing, person-to-person outreach with individuals and groups, etc; or

(b) issue a Discussion Paper and gather the evidence through written submissions and at the same time conduct person-to-person outreach with individuals and groups.

73. In this context, the staff draw attention of the Board members to the factors set out in *Appendix C* (reproduction of paragraphs 24–41 of Agenda Paper 28 for the February 2018 Board meeting).

74. For the goodwill and impairment research project, the following factors are important:

(a) the stage of development (see paragraphs C4–C6);

(b) the significance of change (see paragraphs C7–C10); and

(c) the need for formal consultation (see paragraphs C1–C3).

75. The headroom approach is clearly in the idea generation phase. Furthermore, if feedback from GPF is considered representative of the view of preparers generally, the headroom approach is likely to become controversial. There is a clear need to provide the opportunity for debate about the approach to mature among stakeholders. Accordingly, a Discussion Paper would be the ideal document for the Board to define the problem, explain why the Board considered the headroom approach, explain that the Board is sensitive to the cost concerns and seek feedback.

76. All other changes listed in paragraph 70 are not necessarily new ideas. Those changes are not likely to result in significant differences from existing practice. Having said that, those changes are not yet ready to become specific standard-setting proposals because of the need for more outreach and analysis to understand the costs and establish that the expected benefits exceed the expected costs. Feedback on a Discussion Paper could provide robust evidence on costs and benefits for reasons explained in paragraph C2(a).

77. Furthermore, as explained in paragraph 7 of the paper, the issues are interconnected and the possible answers are interconnected. Feedback on a Discussion Paper could highlight any dependencies that we may have overlooked.

Staff recommendation

78. The staff recommend that the Board issue:

    (a) an Exposure Draft proposing amendments to IAS 36 to:

        (i) remove the explicit requirement to use pre-tax inputs in calculating value in use, and to disclose pre-tax discount rates used; and

        (ii) instead, require an entity to use internally consistent assumptions about cash flows and discount rates, and to disclose the discount rate(s) actually used.

    (b) a Discussion Paper inviting comments on the Board's preliminary views on all other matters considered in the research project.

79. The staff draw the attention of Board members to the Board's decision to propose an amendment to IAS 41 *Agriculture* as part of the Board's next Annual Improvements Cycle.[2] The amendment would remove the requirement for entities to exclude cash flows for taxation when measuring the fair value of biological assets using a present value technique. The Board could consider proposing the amendments to IAS 36 set out in paragraph 78(a) as part of the Board's next Annual Improvements Cycle together with those proposed amendments to IAS 41. The Board will be asked to make that decision at a future meeting.

Question for the Board
Does the Board agree with the staff recommendation in paragraph 78?

[2] The project page of proposed amendments to IAS 41 can be accessed at http://www.ifrs.org/projects/work-plan/taxation-in-fair-value-measurements/

Appendix A
Background on the PIR of IFRS 3

A1. The Board issued a revised version of IFRS 3 in 2008 requiring entities to apply the Standard for annual reporting periods beginning on or after 1 July 2009.

A2. As part of its due process, the Board is required to conduct a PIR once a new Standard or major amendment has been in applied internationally for at least two years. The purpose of a PIR is to ensure that the new Standard or major amendment is working as intended. There is no presumption that a PIR will lead to any changes to a Standard. Depending upon the nature of findings, the Board may consider making minor amendments to the Standard or prepare an agenda proposal for a broader revision of the Standard.

A3. The PIR of IFRS 3 began in 2013, about three years after entities started applying IFRS 3. As part of the PIR, the Board sought feedback on specified questions about:

(a) the definition of business;

(b) fair value measurement in a business combination;

(c) the separate recognition of intangible assets from goodwill;

(d) accounting for negative goodwill;

(e) impairment of goodwill and indefinite-lived intangible assets;

(f) accounting for non-controlling interests;

(g) accounting for step acquisitions and loss of control; and

(h) disclosures.

See Request for Information (issued in January 2014) for more information about the questions asked.

A4. After reviewing the results of the Request for Information, feedback from outreach activities and academic research, the Board assessed some of the topics listed in paragraph A3 as requiring further follow-up. The Board concluded the PIR of IFRS 3 by:

(a) publishing the Report and Feedback Statement in June 2015;

(b) adding to its work plan a maintenance project on the definition of business; and

(c) adding to its work plan a research project covering the following topics:

(i) the separate recognition of intangible assets from goodwill;

(ii) impairment of goodwill and indefinite-lived intangible assets; and

(iii) disclosures.

A5. See Appendix A of Agenda Paper 18A for the December 2017 Board meeting for a summary of stakeholders' feedback received during and after the PIR of IFRS 3.

A6. As part of its 2015 Agenda Consultation, the Board considered whether to add the other topics listed in paragraph A3—fair value measurement in a business combination, accounting for negative goodwill, accounting for non-controlling interests, and accounting for step acquisitions and loss of control—to its work plan. After considering stakeholders' feedback, the Board decided not to add those topics to its work plan.

Appendix B
The Board's tentative decisions so far

B1. The following table (Table 1) summarises the various possible approaches discussed by the Board for improving the application of IAS 36 and for improving disclosures about goodwill and impairment.

Objective	***Possible approaches***	***Board's preferred approach***
Improving effectiveness of impairment testing	Changing the current requirement of using higher of value in use and fair value less costs of disposal to using a single method as the sole basis for determining the recoverable amount of an asset (or a cash−generating unit)	No
	Using the unrecognised headroom of a cash−generating unit (or groups of units) as an additional input in the impairment testing of goodwill	Yes
Simplify the impairment test	Providing relief from the mandatory annual quantitative impairment testing of goodwill	No
	Removing the requirement for an entity to exclude from the value in use calculation cash flows resulting from a future restructuring or a future enhancement.	Yes
	Removing the explicit requirement to use pre-tax inputs to calculate value in use and to disclose the pre-tax discount rates used. Instead, an entity would be required: a. to use internally consistent assumptions about cash flows and discount rates; and b. to disclose the discount rate(s) actually used	Yes
	Allowing goodwill to be tested for impairment at the entity-level or at the level of reportable segments	No

Objective	***Possible approaches***	***Board's preferred approach***
Additional disclosures	Each year, information about the headroom in a cash-generating unit (or groups of units) to which goodwill is allocated for impairment testing	Yes
	Each year, a breakdown of goodwill by past business combination, explaining why the carrying amount of goodwill is recoverable	Yes
	The reasons for paying a premium that exceeds the value of the net identifiable assets acquired in a business combination, key assumptions or targets supporting the purchase consideration and, then subsequently each year, a comparison of actual performance with those assumptions or targets	Yes
	Disclosure of the payback period of an investment in a business combination	No

B2. The following table (Table 2) summarises the staff's assessment of the extent to which each of the project approaches set out in paragraph 9 would meet the intended primary objective and other objectives of the research project. (The intended primary objective of each project approach is highlighted in bold text within square brackets.). This table has been extracted from the staff's assessment in Agenda Paper 18D for the December 2017 meeting.

Table 2	Simplification *Simplify without making the test less robust*	Effectiveness *Improve timing of goodwill impairment*	Better and (or) timely information	Reduces costs or complexity	Remarks
Headroom approach **[effectiveness]**	—	✓✓	✓✓	✗	See Agenda Paper 18C for the December 2017 Board meeting.
Removing restrictions on cash flow projections used in calculating value in use **[simplification]**	✓	✓	—	✓	See Agenda Paper 18B for the January 2018 Board meeting. This approach does not in itself make impairment testing more effective. However, it (a) might mitigate some possible concerns about the costs of applying the headroom approach; and (b) enhances the relevance of the disclosure of headroom.
Not specifying whether the inputs used for calculating value in use are pre-tax or post-tax inputs **[simplification]**	✓	—	✓	✓	See Agenda Paper 18A for the January 2018 Board meeting.
Disclosure of headroom **[improved disclosures]**	—	✓	✓✓	✗	This disclosure could contribute to making the impairment test effective because entities are likely to undertake more rigorous and extensive calculations than they otherwise would.
Breakdown of goodwill by past acquisition **[improved disclosures]**	—	—	✓	✗	This disclosure might help investors in identifying the carrying amount of goodwill relating to business combinations that they consider unsuccessful.
Reasons for payment of premium, key assumptions or targets supporting the purchase consideration and comparison of actual performance with targets **[improved disclosures]**	—	✓	✓✓	✗✗	For this disclosure to be meaningful, an entity would have to disclose commercially-sensitive information. Preparers may therefore hold the view that the costs of making this disclosure outweigh the benefits. This disclosure could serve to alert investors to a risk that goodwill could become impaired, and could highlight areas in which investors might want to question management.

✓✓	Significantly contributing to achieving the desired outcome
✓	Moderately contributing to achieving the desired outcome
—	Neutral effect or not relevant
✗	Moderately detracting from achieving the desired outcome
✗✗	Significantly detracting from achieving the desired outcome

Appendix C
Factors to consider in determining whether a Discussion Paper or an Exposure Draft is appropriate

[Reproduction of paragraphs 24–41 of Agenda Paper 28 for the February 2018 Board meeting. The paragraphs have been renumbered for convenience of referring to those paragraphs in this paper.]

The need for formal consultation

C1. The Board is required to seek formal feedback on new Standards and amendments to Standards. The Board also considers whether to seek public feedback on the evidence gathered in a research project. The nature of the information being sought should determine the approach used.

C2. The Board can consult through the publication of a consultation document, which elicits written submissions, or by conducting person-to-person outreach. The staff observes that:

(a) written submissions are generally based on consultation documents which provide a common articulation of a proposal and can be accessed by any interested party. In addition:

(i) written submissions are generally more considered and detailed than is oral feedback, partly because respondents have a longer period to develop and articulate their responses. Such submissions can be particularly useful when the issues or proposals are complex, because complexity and the resulting nuance can be better conveyed in a written submission. This can allow for a more thorough analysis of stakeholder views.

(ii) written submissions are generally made publicly available, which increases transparency. Any interested party can read the feedback of others and assess for themselves whether we have adequately understood and responded to that feedback.

(b) person-to-person outreach, either with individuals or with groups, may be more dynamic than written consultation, because two-way dialogue can allow for a greater exploration of issues and implications.

However, outreach meetings can provide less detailed input compared to written submissions, which generally set out fuller, considered explanations. In addition, outreach meetings generally:

(i) are narrower in scope than written consultation, because it is limited to people we can arrange meetings with and limited by the time allowed for the meetings. Because of the necessarily limited time for meetings, it can be difficult to ensure that the views gathered are comprehensive.

(ii) provide more subjective input than in a written submission because reporting outreach to the whole Board relies on a summary prepared by the staff.

C3. Although written consultation documents could increase the opportunities for those not obviously affected by a proposal to comment and for the Board to obtain broader views, such opportunities rely on wide document circulation. Accordingly, the Board and staff generally supplement the issuance of a consultation document with outreach, which can be targeted on specific proposals or to specific types of stakeholder. Outreach is particularly needed for users of financial statements, who often do not respond in writing to a consultation document.

The stage of development

C4. Projects evolve over time; the thinking of interested parties and those affected by a project also evolves. A solid understanding and agreement on core topics, before a project is too far advanced, can help create consensus and ultimate acceptability of a new Standard or major amendment. As the project progresses, the Board develops requirements based on underlying concepts and approaches established earlier in the project. Any change to those underlying concepts and approaches requires the implications to be considered for the later decisions and the effect of the changes on the interrelationships between decisions to be re-evaluated. Thus the impact of new ideas becomes progressively more significant. Accordingly, it can be useful to accept wide-ranging discussions and ideas in early stages to ensure there is sufficient evidence to support the approach the Board chooses to take.

C5. Typically, a project would have a number of phases—idea generation, idea implementation and refinement. It can be useful to try to keep these phases distinct. Thus:

(a) a research project is part of the idea generation phase. At this stage, the Board is still defining the problem and scope of the project and considering the possible approaches to address the issue. A Discussion Paper conveys and seeks feedback on the possible approaches.

(b) a standard-setting project is part of the implementation phase. The Board will have selected an approach, and, at this stage is setting out its view of what the accounting requirements should be. An Exposure Draft seeks feedback on specific proposed requirements. Ideally, the proposed requirements should be complete enough for the Board to issue a final Standard based on the Exposure Draft.

(c) the Board issues a final Standard after the refinements phase. At the refinements phase, the Board is considering how to modify the proposed requirements in the light of the feedback.

C6. It can be disruptive to a project, for example, to try to incorporate fundamentally new ideas after the idea generation phase.

The significance of change

C7. In adding a standard-setting project to the Board's agenda, the Board's need to first consult on evidence gathered in a research project is relative to the significance of the accounting-requirement change proposed.

C8. When a change would result in significant differences from existing practice, there is a greater need to consult on the evidence gathered in the research project before adding a standard-setting project to the agenda. This is also the case for changes when there is a high degree of controversy—when there are divergent views about the improvements that need to be made or the best approach to those improvements, there is a greater need for formal consultation.

C9. Formal consultation in the form of a Discussion Paper is useful to ensure that the full range of views is captured, considered and acknowledged, leading to a common understanding of the foundation of future proposals. A Discussion Paper is useful for establishing a foundation for future proposals because it can explore a range of possible approaches and the limitations of each approach relative to the others. The Discussion Paper is particularly useful when there is a range of answers or several interrelated issues to explore. Finally, a Discussion Paper is useful as a change management tool because it provides an opportunity to set out and refine a common articulation of the issues. A common articulation can reduce the risk of instinctual opposition to change, provide the opportunity for debate to mature among stakeholders and bring interested parties together to work towards a consensus about approaches to issues.

C10. In contrast, when the Board has already determined the approach it intends to pursue, and when that approach is generally understood and accepted by interested parties, an Exposure Draft may be appropriate. An Exposure Draft is also more effective than a Discussion Paper for proposals in which the drafting is critical, for example in defining new terms.

The effect on timelines

C11. Formal consultation adds a significant amount of time to projects. The usual minimum comment period for Discussion Papers and Exposure Drafts is 120 days. Following the comment period, the staff needs to analyse the comments and summarise that analysis for the Board to consider in a public meeting. The Board will then deliberate on the issues raised during the consultation and determine how it will proceed. Each consultation step takes two to three years to complete.

C12. While allowing this time for consultation is consistent with the principle of full and fair consultation, there are disadvantages to longer timelines when not needed:

(a) it delays any action to address the issues in financial reporting that caused the Board to start the project. In other words, it delays addressing the needs of users of financial statements. It can also be difficult for interested parties to understand why the Board does not address identified issues sooner.

(b) it may mean that stakeholders become disengaged from a project.

(c) it can create operational difficulties, through lack of continuity of staff and board members.

C13. In some cases, it may be possible for the Board to divide a project into a part that is relatively straightforward and a part that contains more complex issues that require further development. In principle, the relatively straightforward part could be finalised before completing the more complex part. This could be a useful way to achieve improvements in financial reporting on a shorter timeline.

C14. Before deciding to divide a project in this way, the Board needs to consider:

(a) the extent to which the two parts of the project are interrelated. Stakeholders are unlikely to accept changes to Standards if they think that those changes have undesirable implications that have not been debated, or that could be later reversed if the Board were to revisit the issue.

(b) the effect on the overall timeline. Any consultation, even when limited, requires resource for drafting, conducting outreach, analysis and reporting.

(c) the availability of resourcing. Concurrent work on two parts of a project could reduce timelines, but is only possible when there is sufficient staff resource.

Possible pitfalls—re-exposure

C15. The Board's ultimate aim is to achieve improvements to financial reporting as efficiently and effectively as possible. In selecting its approach to consultation, the Board needs to balance the time needed for consultation against the benefits of consultation. Failing to consult appropriately can have the following risks:

(a) insufficient information is obtained to proceed to the next stage, which means that a stage needs to be repeated. For example, when feedback results in significant changes to the scope of content of proposals in an Exposure Draft, the Board may need to re-expose its revised proposals in a revised Exposure Draft.

(b) a Standard or amended Standard is finalised that does not address the issues effectively, leading to a need for further standard-setting in the future.

C16. The requirements for re-exposure are set out in the *Due Process Handbook*:

6.25 In considering whether there is a need for re-exposure, the IASB:

(a) identifies substantial issues that emerged during the comment period on the Exposure Draft and that it had not previously considered;

(b) assesses the evidence that it has considered;

(c) determines whether it has sufficiently understood the issues, implications and likely effects of the new requirements and actively sought the views of interested parties; and

(d) considers whether the various viewpoints were appropriately aired in the Exposure Draft and adequately discussed and reviewed in the Basis for Conclusions.

6.26 It is inevitable that the final proposals will include changes from those originally proposed. The fact that there are changes does not compel the IASB to re-expose the proposals. The IASB needs to consider whether the revised proposals include any fundamental changes on which respondents have not had the opportunity to comment because they were not contemplated or discussed in the Basis for Conclusions accompanying the Exposure Draft. The IASB also needs to consider whether it will learn anything new by re-exposing the proposals. If the IASB is satisfied that the revised proposals respond to the feedback received and that it is unlikely that re-exposure will reveal any new concerns, it should proceed to finalise the proposed requirements.

6.27 The more extensive and fundamental the changes from the Exposure Draft and current practice the more likely the proposals should be re-exposed. However, the IASB needs to weigh the cost of delaying improvements to financial reporting against the relative urgency for the need to change and what additional steps it has taken to consult since the Exposure Draft was published. The use of consultative groups or targeted consultation can give the IASB information to support a decision to finalise a proposal without the need for re-exposure.

C17. Thus, the risk of re-exposure increases:

(a) if insufficient evidence is gathered, which might mean that substantial issues could still emerge during the comment period on the Exposure Draft, which the Board has not previously considered.

(b) if the Board does not obtain enough evidence to allow the various viewpoints to be appropriately aired in the Exposure Draft and adequately discussed and reviewed in the Basis for Conclusions.

C18. It may be tempting to regard an Exposure Draft followed by a re-Exposure Draft as equivalent to a Discussion Paper followed by an Exposure Draft, except with the possibility of finalising a Standard after the first Exposure Draft that does not exist for a Discussion Paper. However, a Discussion Paper is generally a high-level document, while an Exposure Draft must get the details right. This means that the Board's ability to respond to feedback can be more limited after an Exposure Draft compared with a Discussion Paper, as follows:

(a) a Discussion Paper sets out various approaches, whereas an Exposure Draft sets the details of the Board's preferred approach. The development of those details takes place within the context of that approach and may be constrained to that approach. If the Board were to decide to pursue a different approach, all of the details of the approach would need to be re-established and this can be difficult if stakeholders agree with a particular outcome, but not the overall approach. Thus, following an Exposure Draft, it can be difficult to modify the proposals if the modification alters the fundamental approach set out in the Exposure Draft. It can also be more efficient to ensure that an approach is tenable before devoting time to developing the details.

(b) the feedback from a revised Exposure Draft can be difficult to interpret. Because of the burden consultation documents impose on stakeholders, those who agreed with the first Exposure Draft have reduced motivation to reiterate their agreement, and this can mean that the feedback on a revised Exposure Draft may not provide a balanced range of views. A lack of balance in the views obtained could result in decision-making based on incomplete information.