
IASB[®] meeting

Date **December 2022**
Project **Goodwill and Impairment**
Topic **Moving to the standard-setting agenda**
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Purpose and structure

1. The purpose of this paper is to ask the International Accounting Standards Board (IASB) whether it agrees with our recommendation to move the Goodwill and Impairment project from its research programme to its standard-setting work plan.
2. If the IASB decides to add a standard-setting project to its work plan, it also needs to decide whether to set up a consultative group for the project. We think the IASB should also consider whether to update the name of the project to better reflect the matters the project addresses.
3. The paper is structured as follows:
 - (a) summary of staff recommendations (paragraph 4)
 - (b) background on the Goodwill and Impairment project (paragraphs 5–8);
 - (c) moving to the standard-setting work plan (paragraphs 9–30);
 - (d) consultative group (paragraphs 31–32); and
 - (e) the name of the project (paragraphs 33–34).

Summary of staff recommendations

4. We recommend that the IASB:
 - (a) add the Goodwill and Impairment project to its standard-setting work plan;
 - (b) not establish a dedicated consultative group for the project; and
 - (c) change the title of the project to Business Combinations—Disclosures, Goodwill and Impairment.

Background on the Goodwill and Impairment project

5. The IASB added this project to its research programme in response to feedback to the Post-implementation Review (PIR) of IFRS 3 *Business Combinations*. The IASB completed its PIR of IFRS 3 and published the [Report and Feedback Statement](#) on the PIR of IFRS 3 in June 2015.

6. The project objective is to explore whether entities can, at a reasonable cost, provide users of financial statements (users) with more useful information about the business combinations those entities make. To meet this objective the IASB is considering additional disclosure requirements about business combinations, the subsequent accounting for goodwill and other topics related to business combinations such as the recognition of acquired intangible assets.
7. The IASB published the Discussion Paper *Business Combinations—Disclosures, Goodwill and Impairment* in March 2020 which outlined its preliminary views on these topics.
8. The IASB has since been deliberating some of its preliminary views in the light of feedback to the Discussion Paper and other research and outreach. Taking into account the work performed while the project has been on the research programme and the decisions the IASB has made on this project since June 2021, we think the IASB has sufficient information to make a decision on whether to move this project to its standard-setting work plan.

Moving to the standard-setting work plan

9. Paragraph 5.1 of the *Due Process Handbook* states:

In considering whether to add a standard-setting project to the work plan, the IASB or the Interpretations Committee requires the development of a specific project proposal and an assessment against the project criteria outlined in paragraph 5.4...
10. Paragraph 5.2 states that the primary objective of a project proposal is to help the IASB to manage its resources effectively and to prioritise its standard-setting work. The IASB distinguishes between major and narrow-scope projects in its planning to help reduce the risk of committing resources to a project when other projects should have a higher priority.
11. We set out:
 - (a) the criteria in the *Due Process Handbook* for adding a project to the standard-setting work plan (paragraphs 12–13); and
 - (b) why we think those criteria have been met (paragraphs 14–30).

Criteria

12. Paragraph 5.4 of the *Due Process Handbook* states that when adding a standard-setting project to its agenda, the IASB evaluates the merits of adding the project primarily on the basis of the needs of users, while also taking into account the costs of preparing the information. When deciding whether a proposed agenda item will address users' needs, the IASB 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.
13. Paragraph 5.7 of the *Due Process Handbook* also states that the IASB adds a standard-setting project to the work plan only if it concludes that the benefits of the improvements to financial reporting will outweigh the costs.

Meeting the criteria

14. The following sections describe the work we and the IASB have undertaken to assess:
- (a) whether there is a deficiency in reporting (paragraphs 15–17);
 - (b) the importance of any deficiency to users (paragraphs 18–20);
 - (c) the types of entities likely to be affected by the proposals and the pervasiveness of the problem (paragraphs 21–24); and
 - (d) the costs and benefits of the proposals (paragraphs 25–29).

Deficiencies in current reporting

15. The PIR of IFRS 3 identified a number of concerns with the application of IFRS 3 that are being considered in this project:
- (a) Providing users with better information about the subsequent performance of business combinations.
 - (b) Concerns about the effectiveness of the impairment test of cash-generating units containing goodwill in IAS 36 *Impairment of Assets*. The project includes considering whether concerns about the effectiveness of the impairment test could be resolved through improvements to the impairment test and whether to reintroduce amortisation of goodwill.
 - (c) The cost and complexity of the impairment test in IAS 36.
 - (d) Identification and fair value measurement of intangible assets acquired in a business combination such as customer relationships and brand names.
16. The IASB has made some tentative decisions on those areas in the project, based on feedback to the Discussion Paper:
- (a) in [September 2022](#) the IASB tentatively decided to propose adding various disclosure requirements to IFRS 3; and

- (b) in [November 2022](#) the IASB tentatively decided to retain the impairment-only model for the subsequent accounting for goodwill.
17. As noted in Agenda Paper 18B to this meeting, we recommend not considering the intangible assets acquired in a business combination further. If the IASB agrees with our staff recommendation in that paper, and considering the IASB's decisions to date, the project would therefore focus on:
- (a) improving the disclosure requirements in IFRS 3 to better meet user needs; and
- (b) considering whether it is feasible to amend the impairment test in IAS 36 to improve its effectiveness and to simplify its application.

Importance of deficiency to users

18. Business combinations are often large investments that are typically riskier than other types of investment (such as investing in a new item of PPE). Business combinations can cause material changes to an acquiring entity's financial position and performance. The IASB identified the need to provide users with better information about the performance of business combinations as an area of focus in the PIR of IFRS 3.
19. [Agenda Paper 18B](#) to the IASB's April 2021 meeting summarises user feedback on the Discussion Paper. Users were particularly interested in the IASB's preliminary views to improve disclosures about business combinations, with almost all users supporting those preliminary views. Most users said existing disclosure requirements do not provide sufficient useful information. Many users also said that the impairment test in IAS 36 is not effective at recognising timely and adequate impairment losses on goodwill. Users feedback on other topics in the Discussion Paper, for example the subsequent accounting for goodwill, was more split.
20. We think the feedback from users indicates that improving the information about business combinations is important.

Entities affected by the proposals and pervasiveness of the problem

21. Business combinations are undertaken by many entities in many jurisdictions and industries. When business combinations occur, those transactions are often large transactions for the entities involved. Business combinations often result in the acquiring entity recognising goodwill.
22. Paragraph IN1 of the Discussion Paper provides some descriptive statistics of business combinations and goodwill balances globally:

Mergers and acquisitions—referred to as business combinations in IFRS Standards—are often large transactions for the companies involved. These transactions play a central role in the global economy, with deals announced in 2019 totalling in excess of \$4 trillion. According to data extracted from Capital IQ in February 2020, goodwill amounted to \$8 trillion for all listed

companies worldwide, accounting for around 18% of their total equity and 3% of their total assets.

23. Other research demonstrates business combinations are common across several jurisdictions and industries:
- (a) The report [Goodwill: Improvements to Subsequent Accounting and an Update of the Quantitative Study](#) published by the Accounting Standards Board of Japan and the Hong Kong Institute of Certified Public Accountants shows goodwill balances are common in many jurisdictions; and
 - (b) Kroll's [2021 European Goodwill Impairment Study](#) shows that impairment of goodwill is common in many industries.
24. In our view the topics considered in the project are pervasive and affect all types of entities. In particular:
- (a) some of the IASB's proposed new disclosure requirements will be applicable to all entities with 'material' business combinations (although some of the IASB's proposals will affect only a smaller population of 'strategically important' business combinations).
 - (b) the IASB's preliminary views on changes to the impairment test in IAS 36 will affect all entities with goodwill and those that apply the impairment test to other non-financial assets.

Costs and benefits of the proposals

25. As noted in paragraph 6 the objective of the project is to improve the information provided to users about business combinations at a reasonable cost. Therefore, throughout the project to date the IASB has considered how to balance the expected benefits and costs of improvements to financial reporting arising from this project (for example, see paragraphs IN50–IN52 of the Discussion Paper which discuss the costs and benefits of the IASB's preliminary views set out in the Discussion Paper).
26. A detailed effects analysis will be conducted before publishing any Exposure Draft. However, our preliminary assessment is that the benefits of the improvements to financial reporting from this project are likely to outweigh the costs.
27. We think the main benefits (subject to future tentative decisions the IASB makes in this project) include:
- (a) Improving information provided to investors about a business combination and its subsequent performance (through enhancements to the disclosure objectives and requirements in IFRS 3). This will allow users to assess a business combination's performance and management's stewardship of the entity's economic resources. Academic evidence suggests that providing better information to investors reduces an entity's cost of capital¹.

¹ For example, Leuz, C. and Verrecchia, R. E. (2000), 'The Economic Consequences of Increased Disclosure', *Journal of Accounting Research*, 38.

- (b) Amendments to IFRS Accounting Standards to address the criticism from some stakeholders responding to the PIR of IFRS 3 that impairment losses on goodwill are recognised too late, long after the impairment event occurred. For example, amendments to IFRS Accounting Standards to improve the disclosure requirements could help to provide more directly the information some users say comes from the impairment test. In addition, the IASB will also discuss suggestions from some respondents to the Discussion Paper on how to improve the effectiveness of the impairment test in IAS 36.
 - (c) Reduced costs and complexity of performing the impairment test (through simplifications to the impairment test in IAS 36).
28. The IASB's proposals could result in some additional cost for entities, for example, from having to disclose additional information about business combinations. The IASB considered the cost of complying with those proposals and in [September 2022](#), tentatively decided to reduce those costs by:
- (a) requiring some of the additional information to be disclosed for only 'strategically important' business combinations; and
 - (b) exempting entities from disclosing some information in specific circumstances. As a result of the amendments the IASB made to its preliminary views, we think the benefits of the amended disclosure proposals outweigh the cost of disclosing the information.
29. The IASB will continue to consider the expected benefits and cost of the package of proposals resulting from this project throughout the project.

Conclusion

30. Based on our assessment of the criteria, we recommend the IASB move this project from the research programme and add it to its standard-setting work plan.

Consultative group

31. Paragraph 3.59–3.60 of the *Due Process Handbook* require the IASB to consider whether it should establish a consultative group for each major project it adds to its standard-setting work plan. The objective of consultative groups is to give the IASB access to additional practical experience and expertise. The *Due Process Handbook* states that it is not mandatory to have such a group, but if the IASB decides not to have a consultative group for a project, the IASB explains why on the project page and informs the Due Process Oversight Committee.
32. We think a specific consultative group for the Goodwill and Impairment project is unnecessary because:
- (a) The topic is general and affects many entities rather than being sector specific or specialised. The IASB's existing consultative groups have the necessary practical experience and expertise to advise on this project. We have consulted with the Accounting Standards Advisory Forum, Global Preparers Forum and Capital Markets Advisory Committee during the research phase of this project and plan to continue using these groups to provide advice on the project.

- (b) Where particular expertise or experience is required, we think it will be possible to undertake targeted outreach without the need for a specific consultative group (for example, when we tested staff examples illustrating what an entity would be required to disclose applying the preliminary views).

Project title

33. The project's title—'Goodwill and Impairment' could give the impression that the project focuses on only the subsequent accounting for goodwill and does not consider other aspects of the accounting for business combinations. As noted in paragraphs 23–25 of [Agenda Paper 18A](#) to the IASB's June 2021 meeting we think some of the feedback on the project objective might reflect this misunderstanding.
34. Given the scope of the project is wider than the subsequent accounting for goodwill, we think the IASB should change the project title. We recommend titling the project as Business Combinations—Disclosures, Goodwill and Impairment.

Questions for the IASB

Question one for the IASB

Does the IASB agree with our recommendation to remove the Goodwill and Impairment project from the research programme and add it to the standard-setting work plan?

Question two for the IASB

Does the IASB agree with our recommendation to not establish a consultative group for this project?

Question three for the IASB

Does the IASB agree with our recommendation to change the project title to Business Combinations—Disclosures, Goodwill and Impairment?