

Discussion Paper

Business Combinations— Disclosures, Goodwill and Impairment

NZASB – 13 October 2020

The views expressed in this presentation are those of the presenter, not necessarily those of the International Accounting Standards Board or IFRS Foundation.

Polling Question 1

Which stakeholder type do you belong to?

A Preparers (companies)

B Users of financial statements

C Auditors

D Standard-setters

E Academics

F Regulators

G Other

Housekeeping

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The Discussion Paper is available for download on the Goodwill and Impairment project webpage at www.ifrs.org/projects/work-plan/goodwill-and-impairment/.

The Discussion Paper



Objective

To improve the information companies provide to investors, at a reasonable cost, about the acquisitions those companies make.



Timeline



Feedback

The IASB is mainly seeking comments on:

- the usefulness and feasibility of its new disclosure ideas; and
- new evidence or arguments on how to account for goodwill.

Comment deadline 31 December 2020 (changed from 15 September 2020 because of the covid-19 pandemic).

* IFRS 3 introduced the impairment-only approach and replaced IAS 22 which required amortisation.

The IASB's preliminary views

1 Improving disclosures about acquisitions	Require companies to disclose: <ul style="list-style-type: none">• management's objectives for acquisitions; and• how acquisitions have performed against those objectives subsequently. Some targeted improvements to existing disclosures.	
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	<ul style="list-style-type: none">• Present on the balance sheet the amount of total equity excluding goodwill.• Do not change recognition of intangible assets separately from goodwill.	

1 Improving disclosures about acquisitions

What is the issue?



Investors do not get enough information about acquisitions and their subsequent performance

- Such information would allow investors to hold management to account (stewardship)
- IFRS Standards do not specifically require companies to disclose information about the subsequent performance of acquisitions

IASB's preliminary view: require disclosures

At the acquisition date:



- Strategic rationale for acquisition
- Objectives for the acquisition
- Metrics for monitoring achievement of objectives

After the acquisition date:



Performance against objectives

1 Improving disclosures about acquisitions

IASB's preliminary view: Companies should disclose information management uses internally to monitor acquisitions

What metrics should be disclosed?

- No single metric suitable, because business combinations are all different
- Management approach:
 - Less costly to produce
 - Insights into how management manages acquisitions
- Can be operational or financial metrics
- Might be information about combined business where integration occurs

Should all material acquisitions be disclosed?

- Disclosure of all material acquisitions could be onerous for serial acquirers
- Preliminary view: define 'management' as 'chief operating decision maker' (CODM) (IFRS 8 *Operating Segments*)
- Are these the acquisitions that investors would like to know more about?

1 Further improvements to IFRS 3 disclosures

Message from stakeholders

Preliminary view of the IASB

Expected synergies

- Synergies are often an important part of an acquisition.
- Help investors better understand the factors that contributed to the acquisition price.

Require companies to disclose in the year of acquisition the amount, or range of amounts, of synergies expected from an acquisition.

Defined benefit pension liabilities & debt

- Some investors consider these liabilities to form part of the capital employed for acquisitions.
- Needed to assess return on capital employed.

Require companies to disclose the amount of defined benefit pension liabilities and debt of the acquiree at the acquisition date, separately from other classes of liabilities.

Pro-forma information

- Existing disclosure requirements lack guidance, resulting in diversity in practice.
- Preparers question the usefulness of the information, while investors think that the information is important.

Require companies to disclose both actual and pro-forma revenue, operating profit and cash flows from operating activities.

Polling Question 2

Do you think management is monitoring whether a business combination is meeting management's initial expectations?

A Yes

B No

Polling Question 3

Assuming management is monitoring its business combinations, do you think companies should share the information their management is using with investors?

A Yes

B No

Polling Question 4

Do you think companies would disclose the information proposed by the IASB voluntarily if the information is not required to be provided in the financial statements?

A Yes

B No

2 Improving the accounting for goodwill

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What are the issues?

Research undertaken by the IASB



Impairment losses on goodwill are recognised too late

Could be due to:

- too optimistic cash flow estimates; or
- shielding of goodwill from impairment by headroom (see next slide)



The impairment test is complex and costly for companies

A

Can the impairment test be made more effective?

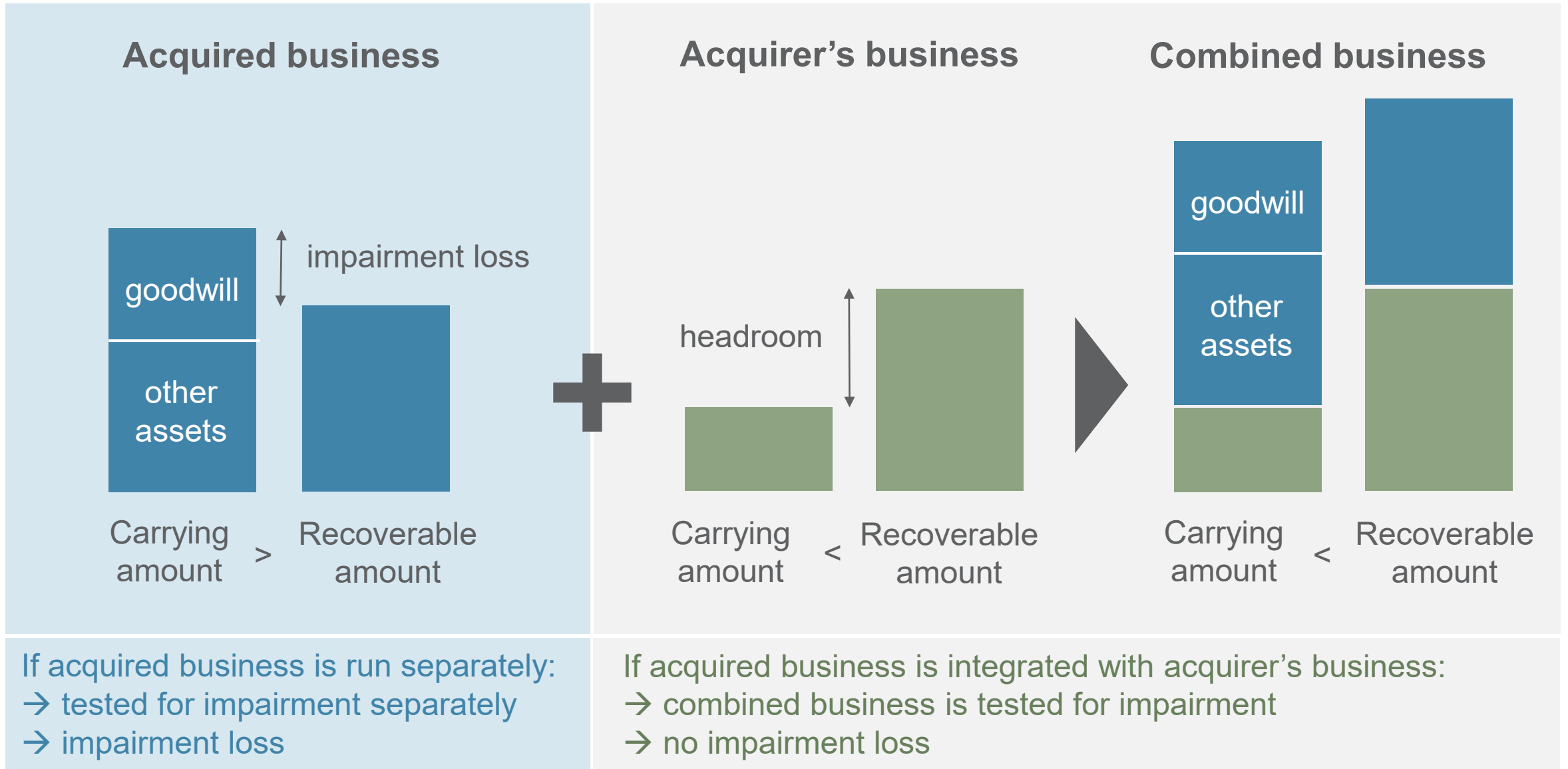
B

Should goodwill be amortised?

C

Can the impairment test be simplified?

② Background—shielding



2 A Can the impairment test be made more effective?

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IASB's preliminary view

No feasible alternative test

- It is not feasible to make the impairment test for goodwill significantly more effective at a reasonable cost to companies.
- Shielding cannot be eliminated because goodwill has to be tested for impairment with other assets.

The test is not intended to test goodwill directly

- The test cannot always signal how an acquisition is performing, but that does not mean that the test has failed.
- When performed well, the test ensures that the carrying amount of the CGU as a whole is recoverable.

Disclosure solution

The disclosure requirements discussed on slides 6–7 could provide information that investors need about the performance of acquisitions.

Polling Question 5

Do you agree with the IASB's preliminary view that the current impairment test in IAS 36 cannot be significantly improved?

- A Yes, goodwill has to be tested with other assets and if cash flows are too optimistic this is an implementation issue
- B No, I have suggestions for an alternative to the current impairment test that is more robust
- C No, I have suggestions for additional guidance which will help improve the application of the current impairment test
- D No, I have suggestions on how the IASB could help address too optimistic cash flows

2 B Amortisation of Goodwill vs Impairment-only

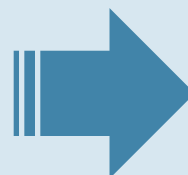
Amortising goodwill	Retaining the impairment-only model
some say...	others say...
Goodwill is overstated, so management is not held to account.	The impairment-only model provides useful confirmatory information to investors.
Amortisation is simple and targets acquired goodwill directly.	Amortisation is arbitrary and would be ignored by many investors.
The impairment test is not working as well as the IASB intended.	If applied well, the impairment test works as the IASB intended, ensuring that, as a group, goodwill and other assets of a business are not overstated.
Goodwill is a wasting asset. Amortisation is the only way to show the consumption of goodwill.	The benefits of goodwill are maintained for an indefinite period, so goodwill is not a wasting asset.
Amortisation would ultimately make the impairment test easier and less costly to apply.	Amortisation would not significantly reduce the cost of impairment testing, especially in the first few years.

2 B Amortisation of Goodwill vs Impairment-only

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IASB's preliminary view

There is no compelling evidence that amortisation would significantly improve financial reporting



Retain the impairment-only approach



The IASB majority was small. Stakeholders are invited to provide new arguments to help the IASB decide how to move forward on this topic.

Polling Question 6

Has your view on the subsequent accounting for goodwill (impairment-only vs amortisation) changed since 2004, when IFRS 3 was issued?

A Yes, I used to support impairment-only and I now support amortisation

B Yes, I used to support amortisation and I now support impairment-only

C No, I have always supported impairment-only

D No, I have always supported amortisation

2C Simplifying the impairment test

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Relief from an annual impairment test



Having to perform the test annually, even when they have no reason to suspect an impairment has occurred, adds unnecessary cost



- Remove requirement to test CGUs containing goodwill for impairment at least annually.
- Companies must still assess whether there is any indicator of impairment, and perform the impairment test if there is.

Simplifying value in use estimates



IAS 36 contains certain restrictions on value in use that add cost and complexity to the test, and deviates from common industry practice



- Remove restriction on including some cash flows in value in use estimates.
- Cash flow forecasts still need to be reasonable and supportable.
- Allow use of post-tax discount rates and post-tax cash flows.

Polling Question 7

What concern(s), if any, do you have about the IASB's preliminary view that it should adopt an indicator-based impairment test for goodwill?

- A Companies might not be able to identify an indicator of impairment when an impairment has occurred
- B Expertise in performing the impairment test might be lost if not performed regularly
- C It provides more opportunity for companies to avoid impairments if they so wish; for example, auditors will find it harder to challenge indicator reviews
- D Performing a review for indicators is just as costly as performing the test
- E I have no concerns (or the benefits outweigh my concerns); I agree with the IASB's preliminary view to adopt an indicator-based impairment test for goodwill

3 Presenting total equity excluding goodwill

XYZ Group – Statement of financial position as at 31 December 20X0

Property, plant and equipment	1,000
Goodwill	<u>2,000</u>
Total non-current assets	3,000
Inventories	1,000
Trade receivables	2,000
Cash and cash equivalents	<u>3,000</u>
Total current assets	<u>6,000</u>
Total assets	<u>9,000</u>
Long-term borrowings	1,000
Deferred tax	<u>2,000</u>
Total non-current liabilities	3,000
Trade and other payables	<u>3,000</u>
Total current liabilities	<u>3,000</u>
Total liabilities	<u>6,000</u>
Share capital	1,000
Retained earnings	<u>2,000</u>
Total equity	<u>3,000</u>
Total equity and liabilities	<u>9,000</u>
Total equity excluding goodwill	<u>1,000</u>

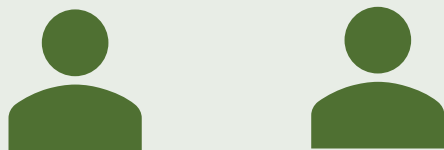
Goodwill is different from other assets because it:

- can only be measured indirectly; and
- cannot be sold separately.

Presenting **total equity excluding goodwill** on the balance sheet helps to make this amount **more prominent**, drawing investors' attention to companies whose goodwill constitutes a significant portion of their net assets.

3 Intangible assets

Separate recognition helps to explain what companies have bought. It also ensures that intangible assets with a finite useful life are recognised separately and amortised.



Separate recognition does not provide useful information, because:

- similar intangible assets are not recognised if generated internally; and
- some intangible assets are difficult to value.

Existing requirements



All identifiable intangible assets acquired in a business combination need to be recognised separately.

Board's preliminary view

- No compelling evidence that requirements in IAS 38 should be amended.
- Considering whether to align the accounting treatments for acquired and internally generated intangible assets is beyond the scope of this project.

A balanced package

Possible changes the IASB considered	Objectives		IASB's preliminary view
	More useful information	Reduce cost	
1 Improve disclosures about acquisitions	✓	✗	Yes, change
2 Amortise goodwill	✗	✓	No, do not change
Provide relief from annual quantitative impairment test	...	✓	Yes, change
Amend how value in use is estimated	✓	✓	Yes, change
3 Present total equity excluding goodwill	✓	...	Yes, change
Include some intangible assets in goodwill	✗	✓	No, do not change

 In line with objective
  In conflict with objective
 ... No significant impact

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