IFRS® Foundation

Discussion Paper

Business Combinations—
Disclosures, Goodwill and Impairment

Contents

Project background & overview

The Discussion Paper

Objective

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

Timeline

2004	2013–2015	2015–present	March 2020
IFRS 3 issued*	PIR of IFRS 3	Goodwill and Impairment project	Discussion Paper

Feedback

The Board 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.

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

Stakeholders' feedback from the PIR of IFRS 3 includes:

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

The impairment test is complex and costly for companies

Impairment losses on goodwill are recognised too late

Goodwill should be amortised. It has been paid for and so, sooner or later, it should have an impact on profit or loss

It is difficult for companies to account for intangible assets such as customer relationships and brands separately from goodwill

The Board's preliminary views

1 Improving disclosures about acquisitions	Require companies to disclose: • 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	• Present on the balance sheet the amount of total equity excluding goodwill. • Do not change recognition of intangible assets separately from goodwill.	

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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

➊ Improving disclosures about acquisitions

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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.

Board'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

Board’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 For how long should information be provided?

For as long as management monitors the acquisition

What if the acquired business is integrated with the existing business?

Companies should disclose the metrics the CODM uses for monitoring; these may be about the combined business.

What if the CODM changes the metrics they use for monitoring?

Companies should disclose the new metrics and the reasons for the change.

At acquisition date	
if monitored by CODM disclose objectives	if not monitored by CODM disclose reason for not monitoring

Within 2 years*	
if monitoring continues disclose performance against objectives	if monitoring ceases disclose reason for ceasing to monitor

After 2 years*	
if monitoring continues disclose performance against objectives	if monitoring ceases no further disclosure needed

*Two full years after the year of acquisition

Should this information be in management commentary?

Board's preliminary view: Companies should disclose information about acquisitions and their subsequent performance in financial statements

What concerns do stakeholders have?

- Management's view
- Information might not be prepared in accordance with IFRS
- Information may be forward looking

Why include in financial statements?

- Management commentary does not always include information about acquisitions
- Management commentary is not always available to users of financial statements

Things to consider

- What information could a company report in management commentary it cannot in financial statements?
- Would companies provide information about the subsequent performance of acquisitions if it were encouraged, not required?

Is this forward looking information?

Board's preliminary view: The information discussed in the Discussion Paper is not forward looking.

Target at time of acquisition

Management's historic aim at the time of the acquisition

Forecast when publishing the report

A current expectation or prediction of future performance

Things to consider

What legislation in your jurisdiction addresses forward-looking information? In what way does it restrict management's ability to describe its targets in financial statements?

Integration

Stakeholders say	Board's preliminary view
Integration may make it difficult to isolate performance	Management might plan to monitor the subsequent performance of the acquisition using information about the combined business. If so, disclosure would therefore use that combined information.
Acquisitions might not be monitored if integration happens quickly	Even when an acquired business has been integrated, it is assumed management understands how the acquisition is performing, at least in the early period. If management stop monitoring an acquired business before the end of the second full year after the year of acquisition, it would disclose that fact.

Things to consider	In your experience, how are acquisitions monitored by management when integration occurs?

Polling Question 2

Do you think management should share any information they have about the subsequent performance of acquisitions with investors?

A Yes

B No

C N/A, management do not track the subsequent performance of acquisitions and therefore do not have this information

Polling Question 3

Do you think the information on subsequent performance should be in management commentary?

A Yes, because it is forward-looking. The information should be disclosed in management commentary because of the risk of litigation

B Yes, because the information is difficult to audit

C Yes, because companies should have flexibility over what information to provide because it could be commercially sensitive

D Yes, because of some other reason

E No, I think the information should be included in the financial statements

Other concerns heard so far

	Message from stakeholders	Preliminary view of the Board
Commercial sensitivity	• May provide competitors with information that would not otherwise be available. • May give away future acquisition targets, driving up any future acquisition price.	• Not a sufficient reason to prevent disclosure of information investors need. • Users want a follow-up on information already provided at the time of acquisition.
Auditability	• Some stakeholders are concerned that the information a company discloses would not be auditable.	Expect that auditors can confirm information: • is used by management • has a clear basis of preparation; and • faithfully represents performance.

Things to consider

What information do you consider commercially sensitive and why?

1 Further improvements to IFRS 3 disclosures

	Message from stakeholders	Preliminary view of the Board
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 4

Do you think companies estimate the value of any material synergies when they acquire a business?

A Yes, I think companies make these estimates in order to determine the price they are willing to pay for a business

B No, I think companies only make these estimates after an acquisition has been completed

C No, I do not think companies make estimates of synergies

❷ Improving the accounting for goodwill

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2 Improving the accounting for goodwill

What are the issues?	Research undertaken by the Board

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)

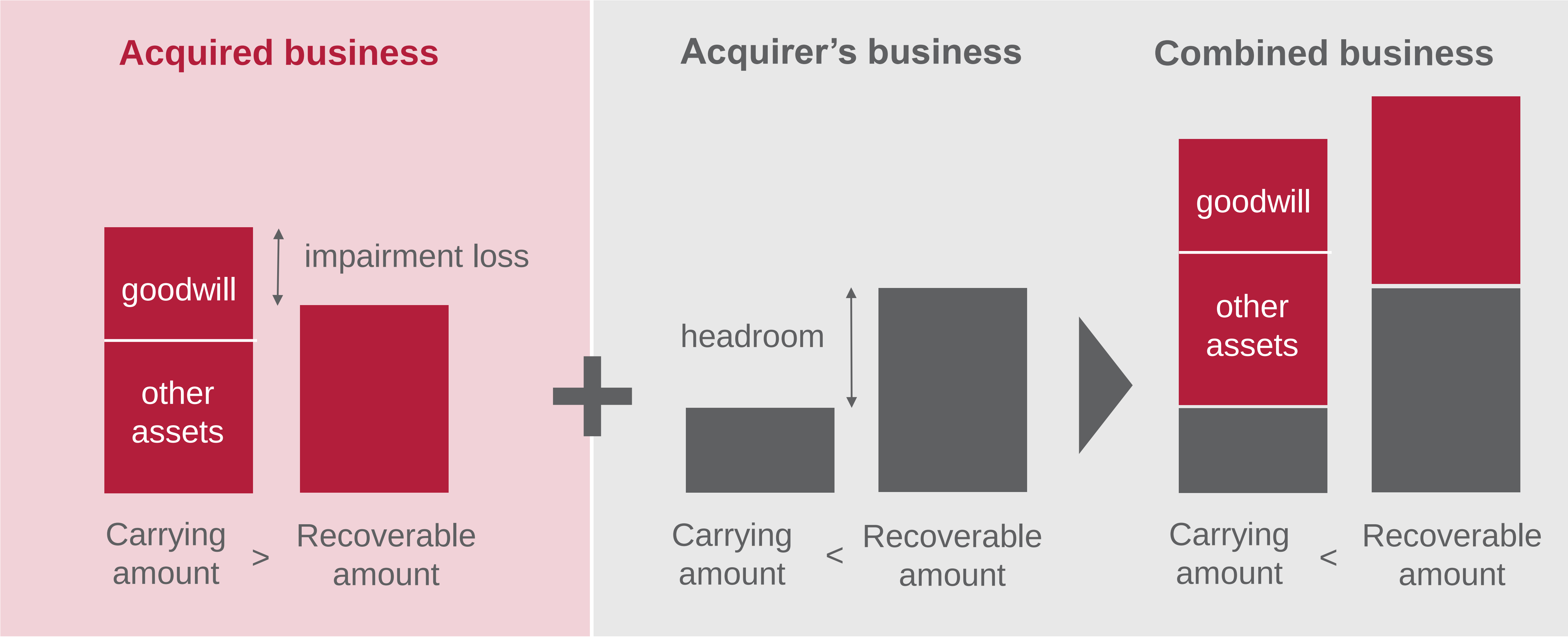
The impairment test is complex and costly for companies

A. Can the impairment test be made more effective?

B. Should goodwill be amortised?

C. Can the impairment test be simplified?

❷ Background—shielding



If acquired business is run separately:
→ tested for impairment separately
→ impairment loss

If acquired business is integrated with acquirer's business:
→ combined business is tested for impairment
→ no impairment loss

2 A Can the impairment test be made more effective?

Board's preliminary view

No feasible alternative test	The test is not intended to test goodwill directly	Disclosure solution
• 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 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.	The disclosure requirements discussed on slides 9–10 could provide information that investors need about the performance of acquisitions.

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 Board intended.	If applied well, the impairment test works as the Board 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.

❷ Ⓑ Amortisation of Goodwill vs Impairment-only

Board's preliminary view

There is no compelling evidence that amortisation would significantly improve financial reporting → **Retain the impairment-only approach**

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

Polling Question 5

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

2 C Simplifying the impairment test

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 6

What concern(s), if any, do you have about the Board’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 agree with the Board’s preliminary view as the benefits outweigh the concerns I might have

❸ Other topics

❸ Other topics

Presenting total equity before goodwill	Intangible assets
Goodwill is different from other assets because it: • can only be measured indirectly; and • cannot be sold separately.	Some believe that recognising these assets separately helps explain what the company has bought in an acquisition. Others think that the information is of limited use.
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.	In the Board's view: • there is no compelling evidence to change existing requirement; and • aligning the accounting treatment for all intangible assets is beyond the scope of this project.

Summary—package of preliminary views

A balanced package

		Objectives		Board'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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