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**Our Ref: 2020/O/C1/IASB/MS/143**

**RE: DP/2020/1 - Business Combinations-Disclosures, Goodwill and Impairment**

Dear International Accounting Standards Board (IASB) Members,

The International Organization of Securities Commissions (IOSCO) Committee on Issuer Accounting, Auditing and Disclosure (Committee 1) thanks you for the opportunity to provide our comments on the Discussion Paper *Business Combinations-Disclosures, Goodwill and Impairment* (“Discussion Paper”).

IOSCO is committed to promoting the integrity of the international markets through promotion of high-quality accounting standards, including rigorous application and enforcement. Members of Committee 1 seek to further IOSCO’s mission through thoughtful consideration of accounting and disclosure concerns and pursuit of improved transparency of global financial reporting. Unless otherwise noted, the comments provided herein reflect the consensus among members of Committee 1 and are not intended to include all the comments that might be provided by individual securities regulator members on behalf of their respective jurisdictions.

### **General Observations**

Business combinations can be large transactions that may result in the recognition of a significant amount of goodwill.<sup>1</sup> The risk of unrecognised impairment on accumulated goodwill balances arising from these business combinations is one of the top priority issues among members of Committee 1. As such, we support the Board’s objective to explore whether companies could provide investors with more useful information through additional disclosures about business acquisitions and / or changes to the accounting model for goodwill, and we believe this is a topic of priority for financial reporting.

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<sup>1</sup> Research shows that goodwill can constitute anywhere from 20 – 60% of the consideration paid in a business combination depending on the industry and market in which the acquisition occurs. See, for example, Ryan, “Purchase Price Allocation to Goodwill Drops,” *CFO* (September 2013); Carvalho, Rodrigues, and Ferreira, “The Recognition of Goodwill and Other Intangible Assets in Business Combinations – The Portuguese Case,” *Australian Accounting Review* (2016).



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From the viewpoint of investor protection, it is crucial that application of financial reporting standards results in fair presentation of the financial position, performance and cash flows of an issuer. Goodwill should not be presented in excess of its recoverable amount on an issuer's statement of financial position, and the recognition of impairment losses should be timely.

Poor or absent disclosure of the key assumptions underlying the impairment of non-financial assets is one of the top issues for enforcers. We believe there is room for improvement regarding the information provided by issuers about goodwill. Such improvement could include disclosure for a so called "close call" when no impairment is recognised but there was very little "cushion" when an impairment test was conducted. In theory, the sensitivity disclosures required in IAS 36 could provide similar information, however members would like to see a more explicit disclosure requirement in the case of a "close call".

Another way to see the importance of this issue is through the requirement for auditors to identify Key Audit Matters (KAM) under International Standards on Auditing (ISA) or Critical Audit Matters (CAM) under the PCAOB Auditing Standards within the auditor's reports. Many auditors identify goodwill impairment as one of the significant matters they consider during the course of their audit and this issue is communicated to audit committees as well. The requirement to identify CAMs began last year, and some of the early examples of the new auditors' reports show that goodwill impairment is among the most frequently communicated CAM within the auditor's reports.<sup>2</sup> This shows a strong focus among auditors and audit committees on this issue.

We also note that the U.S. Financial Accounting Standards Board (FASB) is considering similar issues under U.S. GAAP. In this regard, we urge the IASB to work as collaboratively as possible with the FASB both in terms of timing of the project and in an effort to achieve or maintain outcomes that are as converged as possible. The G20 leaders have emphasized the importance of achieving a single set of high-quality global accounting standards that are consistently and rigorously applied. We believe the argument by the G20 is still relevant for this issue and therefore we call on the IASB and the FASB to increase their efforts to achieve convergence.

Although members support many of the preliminary views identified in the Discussion Paper by the Board, we have identified items within that should to be reconsidered, require clarification, or need additional guidance in order to support consistent application.

Our detailed feedback on each section of the Discussion Paper is provided below.

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<sup>2</sup> PCAOB Critical Audit Matters Spotlight, <https://pcaobus.org/Documents/CAMs-Spotlight.pdf> and PCAOB Interim Analysis Reports: Evidence on the Initial Impact of Critical Audit Matter Requirements, <https://pcaobus.org/EconomicAndRiskAnalysis/pir/Documents/ARM-Interim-Analysis-Report.pdf>



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## Responses to the Board's Questions

### Question 1

Paragraph 1.7 summarises the objective of the Board's research project. Paragraph IN9 summarises the Board's preliminary views. Paragraphs IN50–IN53 explain that these preliminary views are a package and those paragraphs identify some of the links between the individual preliminary views. The Board has concluded that this package of preliminary views would, if implemented, meet the objective of the project. Companies would be required to provide investors with more useful information about the businesses those companies acquire. The aim is to help investors to assess performance and more effectively hold management to account for its decisions to acquire those businesses. The Board is of the view that the benefits of providing that information would exceed the costs of providing it.

- (a) Do you agree with the Board's conclusion? Why or why not? If not, what package of decisions would you propose and how would that package meet the project's objective?
- (b) Do any of your answers depend on answers to other questions? For example, does your answer on relief from a mandatory quantitative impairment test for goodwill depend on whether the Board reintroduces amortisation of goodwill?  
Which of your answers depend on other answers and why?

### **Response:**

Committee members generally agree with the disclosure proposals, specifically with the Board's intent to require companies to disclose more information about the material businesses they acquire. Such disclosures about material acquisitions are beneficial to investors, providing more decision-useful information regardless of whether an impairment-only model is retained or amortisation is reintroduced. However, we also recognise there could be challenges associated with providing certain types of information depending on securities laws in different jurisdictions.

Although committee members generally share the concern about the substantial accumulation of goodwill and the risk of 'too little too late' when it comes to the determination of the impairment of goodwill, there are mixed views about whether to keep an impairment-only model or to reintroduce amortisation. Some members request that the IASB further analyse and consider improvements to the impairment test (IAS 36) before discussing or considering the reintroduction of amortisation. (Please refer to specific comments provided to later in Question 7.) Other members consider that the reintroduction of amortisation is an urgent matter and the Board should implement it as soon as possible in order to improve financial statements' reliability and usefulness.

With respect to changes to the impairment model, most members are concerned with the removal of the annual impairment test and relying on a solely trigger-based test because such changes will present



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potential enforceability challenges in some jurisdictions. These members do not necessarily oppose such change but believe it should be accompanied by other considerations to provide for greater enforceability. However, some members feel application of a model with a solely trigger based test will not be as robust as the discussion paper does not provide significant improvements to the current impairment test, and does not propose to update the existing indicators of impairment in IAS 36 which are not sufficiently robust. As such, removing the requirement for an annual test could make impairment tests less robust. Other members believe this issue could be addressed by requiring an annual impairment test if the estimated useful life is over 15 or 20 years. (Please refer to specific comments provided to later in Question 9.)

While we do not necessarily oppose other potential changes suggested in the Discussion Paper, we support proposals that will reduce the costs of complying with accounting standards as long as the changes do not result in loss of material information for investors and enforceable principles for regulators.

## Question 2

Paragraphs 2.4–2.44 discuss the Board’s preliminary view that it should add new disclosure requirements about the subsequent performance of an acquisition.

- (a) Do you think those disclosure requirements would resolve the issue identified in paragraph 2.4—investors’ need for better information on the subsequent performance of an acquisition? Why or why not?
- (b) Do you agree with the disclosure proposals set out in (i)–(vi) below? Why or why not?
  - (i) A company should be required to disclose information about the strategic rationale and management’s (the chief operating decision maker’s (CODM’s)) objectives for an acquisition as at the acquisition date (see paragraphs 2.8–2.12). Paragraph 7 of IFRS 8 Operating Segments discusses the term ‘chief operating decision maker’.
  - (ii) A company should be required to disclose information about whether it is meeting those objectives. That information should be based on how management (CODM) monitors and measures whether the acquisition is meeting its objectives (see paragraphs 2.13–2.40), rather than on metrics prescribed by the Board.
  - (iii) If management (CODM) does not monitor an acquisition, the company should be required to disclose that fact and explain why it does not do so. The Board should not require a company to disclose any metrics in such cases (see paragraphs 2.19–2.20).
  - (iv) A company should be required to disclose the information in (ii) for as long as its management (CODM) continues to monitor the acquisition to see whether it is meeting its objectives (see paragraphs 2.41–2.44).



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- (v) If management (CODM) stops monitoring whether those objectives are being met before the end of the second full year after the year of acquisition, the company should be required to disclose that fact and the reasons why it has done so (see paragraphs 2.41–2.44).
- (vi) If management (CODM) changes the metrics it uses to monitor whether the objectives of the acquisition are being met, the company should be required to disclose the new metrics and the reasons for the change (see paragraph 2.21).
- (c) Do you agree that the information provided should be based on the information and the acquisitions a company's CODM reviews (see paragraphs 2.33–2.40)? Why or why not? Are you concerned that companies may not provide material information about acquisitions to investors if their disclosures are based on what the CODM reviews? Are you concerned that the volume of disclosures would be onerous if companies' disclosures are not based on the acquisitions the CODM reviews?
- (d) Could concerns about commercial sensitivity (see paragraphs 2.27–2.28) inhibit companies from disclosing information about management's (CODM's) objectives for an acquisition and about the metrics used to monitor whether those objectives are being met? Why or why not? Could commercial sensitivity be a valid reason for companies not to disclose some of that information when investors need it? Why or why not?
- (e) Paragraphs 2.29–2.32 explain the Board's view that the information setting out management's (CODM's) objectives for the acquisition and the metrics used to monitor progress in meeting those objectives is not forward-looking information. Instead, the Board considers the information would reflect management's (CODM's) targets at the time of the acquisition. Are there any constraints in your jurisdiction that could affect a company's ability to disclose this information? What are those constraints and what effect could they have?

**Response:**

Committee members generally agree with the proposal related to the new disclosure requirements about the subsequent performance of a material business combination.

We believe that the disclosure requirements suggested by the Board would provide more information to investors about the strategic rationale and management's objectives for material acquisitions; such information often is not transparent today. Additionally, using an approach to disclosures based on information used by management to monitor and evaluate the subsequent performance of the acquired operations is likely to result in useful information that is more informative to investors, and at a reasonable cost to preparers. We suggest the IASB include examples of potential disclosures, but clearly indicate that they are only examples and are not intended to be a checklist since actual disclosures will be predicated on the information used by the CODM in the specific fact pattern. The IASB also could consider putting boundaries on the metrics so that it does not end up being a basis for proliferation of non-GAAP financial measures.



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In addition to the proposed new disclosure requirements, some members believe that information about the estimated time necessary to recover the investment in the acquired business would be relevant to investors in order to further evaluate the subsequent performance of an acquisition. Similar to the expectation expressed in paragraph 2.66 of the Discussion Paper regarding management having made an estimate of expected synergies in agreeing to the price of an acquired business, we would expect management to have an estimated time for the pay back period of the investment in many cases. Some members are also in favour of requiring disclosure of how issuers calculated the pay back period as issuers can apply multiple approaches to determining the recovery period.

Some members suggest the IASB should require disclosure of the percentage that goodwill represents of the total acquisition price as part of its discussion of the strategic rationale for the acquisition. In practice, these members have seen many acquisitions in which goodwill represents a significant amount of the acquired net assets recognised in the acquirer's statement of financial position. In many of these cases, the goodwill was impaired a few years later.

We generally agree with the disclosures proposed in Question 2 (b) (i) – (vi). We believe that use of the term CODM is reasonable since it is already a familiar concept in IFRS 8. Furthermore, using the same metrics as are used by the CODM may decrease the operational burden or cost as there would be no need to create additional information solely for external reporting. While we support the use of the CODM perspective to monitor objectives and expected synergies as this information could be relevant for investors in assessing the acquisition and the assumptions included in the goodwill impairment test, we observe that there have been challenges in the past with the application of the CODM model for IFRS 8 purposes that may create similar challenges for the disclosures contemplated in the discussion paper, as further discussed below.

Specifically, some members feel that requiring disclosures only for acquisitions monitored by the CODM may result in investors not receiving information on some material acquisitions and this could lead to enforcement challenges. These members are concerned that a company could omit disclosure if management asserts that certain acquisitions are not monitored by or reported to the CODM, or that management may be biased to only report “good news”. In other words, a company may cease monitoring the performance of an acquisition rather than disclosing negative performance when the acquisition is not performing as well as expected. Some members also report that there have been challenges in the past with issuers representing that the CODM does not receive certain information for IFRS 8 purposes and therefore the disclosure is not provided. As such, these members have some concerns about relying on the CODM criteria as the trigger to make the disclosures proposed in the Discussion Paper and are of the view that the standards around the CODM could be enhanced further in the future. As to the proposals contained in the Discussion Paper, some members would like to see further disclosures such as synergies and workforce in place in addition to information monitored by management for acquisitions generating material goodwill which may not be monitored by the CODM. Other members, however, agree with the Board's discussion and reasoning contained in paragraph 2.20 of the Discussion Paper.



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In addition, some members have raised questions about the duration of time for monitoring an individual acquisition and the availability of information in subsequent periods. Although paragraph 2.45 of the Discussion Paper only asks for additional disclosure if the CODM stops monitoring its objectives for an acquisition before the end of the second full year after the year of acquisition, some members believe this minimum period for monitoring is too short. These members feel that it would be better that when management stops monitoring whether its objectives for the acquisition are met, issuers should disclose that fact and the reasons why it has done so, even if it happens after the second full year after the year of acquisition. Some other members also believe there is a need for disclosure as long as an acquisition is within the pay back period and issuers should disclose if a significant acquisition is no longer being monitored by the CODM even after the second full year after the year of acquisition. Furthermore, we expect to see more guidance in relation to disclosures on the acquisition's subsequent performance and the length of time that this disclosure should continue in order to avoid the disclosure of irrelevant or boilerplate information.

For the reasons described above, we generally agree with the Board's proposal to base the disclosure requirements on the information reviewed by the CODM for purposes of monitoring and evaluating the performance of the acquired operations. However, some members note that management reorganises its segments as it integrates the new business into its existing operations in the case of many material acquisitions. These members believe that the Board should consider how these disclosures might need to be modified or adjusted as the business is being integrated and segments are in the process of being reorganised but a new segment structure has not yet been put in place.

Commercial sensitivity should not prevent companies from disclosing information about management's objectives for an acquisition. Although concerns over commercial sensitivity are likely more prevalent with publicly listed companies as opposed to private companies, it is important for public companies to have transparency. When a company accesses the public capital markets, it is accepting that transparency will be required to continue as a listed company. Additionally, listed companies would have to provide information to investors regarding their objectives for acquisitions in many jurisdictions. For material acquisitions, management would typically discuss with the board of directors its strategic rationale for the acquisition. In circumstances where a regulatory filing, offering document, or other public filing is prepared, it is likely that the strategic rationale will be described in the public document as well. In this regard, it may also be relevant to consider BC 43-44 of IFRS 8 that discusses the Board's view that a "competitive harm" exemption would be inappropriate, in the context of segment disclosures. Moreover, some members are concerned that issuers may start citing commercial sensitivity to potentially circumvent other disclosure requirements in IFRSs if the Board permits issuers not to disclose information because of commercial sensitivity in this case. We acknowledge that commercial sensitivity plays a role in the cost and benefit analysis of disclosure requirements and we would encourage the Board to give that consideration and provide guidance as it develops its disclosure requirements.

We support the Board's proposals and most members agree with the Board's conclusions that the disclosure proposal is not asking for management to provide forward-looking information, rather, it is



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just asking management to disclose the judgements made at the time of the acquisition and the information used by management to evaluate the success of the acquisition. However, in some jurisdictions, the proposed disclosure pertaining to management's objectives, including the metrics for measuring the progress of objectives and targets, would be considered forward-looking information under local securities legislation. Though these members support the Board's preliminary view, in these jurisdictions, the inclusion of this information would trigger additional disclosures pertaining to forward-looking information.

Since the disclosure proposals are based on information provided to the CODM, we are not aware of any constraints or impediments to disclosing this information. On the other hand, some members are concerned that information disclosed within the financial statements may include certain non-GAAP metrics like synergies and those members believe such information should not be included in the financial statements but, rather, should be disclosed outside financial statements.

### Question 3

Paragraphs 2.53–2.60 explain the Board's preliminary view that it should develop, in addition to proposed new disclosure requirements, proposals to add disclosure objectives to provide information to help investors to understand:

- the benefits that a company's management expected from an acquisition when agreeing the price to acquire a business; and
- the extent to which an acquisition is meeting management's (CODM's) objectives for the acquisition.

Do you agree with the Board's preliminary view? Why or why not?

### Response:

We agree with the Board's proposal to include disclosure objectives about information needed to help investors understand the benefits that management expected from an acquisition when agreeing the price to acquire a business and the extent to which an acquisition is meeting management's objectives, subject to our concerns expressed in our response to Question 2.

Standards-level disclosure objectives should capture the general intention of disclosures and are meant to guide the Board when drafting specific requirements and management in fulfilling its disclosure responsibilities. This approach is also consistent with the feedback on the Discussion Paper - Disclosure Initiative - Principles of Disclosure (March 2017).





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#### Question 4

Paragraphs 2.62–2.68 and paragraphs 2.69–2.71 explain the Board’s preliminary view that it should develop proposals:

- to require a company to disclose:
  - a description of the synergies expected from combining the operations of the acquired business with the company’s business;
  - when the synergies are expected to be realised;
  - the estimated amount or range of amounts of the synergies; and
  - the expected cost or range of costs to achieve those synergies; and
- to specify that liabilities arising from financing activities and defined benefit pension liabilities are major classes of liabilities.

Do you agree with the Board’s preliminary view? Why or why not?

#### **Response:**

We generally agree with the proposals, but this disclosure requirement should be complemented with requirements in subsequent periods to disclose whether or not the company fulfilled its expectation about synergies previously disclosed in the financial statements.

We are aware that acquisitions can be financed in a number of ways including new borrowing by the acquirer, assumption of the target’s debt, new borrowing that is transferred to the target at closing, and seller-financed borrowing, among others. With respect to the liabilities arising from financing activities, we would encourage the Board to think holistically about that disclosure requirement such that different forms or structures used to raise debt and capital do not result in differences in whether disclosures are or are not required.

We also support the separate disclosure of defined benefit pensions and financing liabilities as those have specifically been asked for by investors.

#### Question 5

IFRS 3 Business Combinations requires companies to provide, in the year of acquisition, pro forma information that shows the revenue and profit or loss of the combined business for the current reporting period as though the acquisition date had been at the beginning of the annual reporting period.

Paragraphs 2.82–2.87 explain the Board’s preliminary view that it should retain the requirement for companies to prepare this pro forma information.

(a) Do you agree with the Board’s preliminary view? Why or why not?



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- (b) Should the Board develop guidance for companies on how to prepare the pro forma information? Why or why not? If not, should the Board require companies to disclose how they prepared the pro forma information? Why or why not?

IFRS 3 also requires companies to disclose the revenue and profit or loss of the acquired business after the acquisition date, for each acquisition that occurred during the reporting period.

Paragraphs 2.78–2.81 explain the Board’s preliminary view that it should develop proposals:

- to replace the term ‘profit or loss’ with the term ‘operating profit before acquisition-related transaction and integration costs’ for both the pro forma information and information about the acquired business after the acquisition date.  
Operating profit or loss would be defined as in the Exposure Draft General Presentation and Disclosures.
- to add a requirement that companies should disclose the cash flows from operating activities of the acquired business after the acquisition date, and of the combined business on a pro forma basis for the current reporting period.

- (c) Do you agree with the Board’s preliminary view? Why or why not?

**Response:**

We agree with the IASB that it should retain the pro forma information and the disclosures about the acquired business after the acquisition.

We also support the development of additional guidance, but recommend that the Board not be too prescriptive, in order to avoid the inconsistencies in methodologies applied by preparers (e.g. basis for recurring performance, one-off items, seasonality, acquisition-related costs and integration costs, etc.). Therefore, it might be useful for the Board to develop high-level objectives for the preparation of the pro forma information along with disclosure requirements on how the information has been prepared by management. Furthermore, some members feel that there is a need for a clearer definition or relabeling of “pro forma” as the pro forma information in some jurisdictions is quite specific and using the term pro forma in the financial statements may confuse users.

We agree to replace the term ‘profit or loss’ with the term ‘operating profit before acquisition-related transaction and integration costs’ and to add a requirement to disclose the cash flows from operating activities of the acquired business after the acquisition date, and of the combined business on a pro forma basis for the current reporting period. However, some members believe that more guidance would be useful on the nature of “acquisition-related costs and integration costs” in order to enhance comparability in the calculation of the metric required.



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#### Question 6

As discussed in paragraphs 3.2–3.52, the Board investigated whether it is feasible to make the impairment test for cash-generating units containing goodwill significantly more effective at recognising impairment losses on goodwill on a timely basis than the impairment test set out in IAS 36 Impairment of Assets. The Board’s preliminary view is that this is not feasible.

- (a) Do you agree that it is not feasible to design an impairment test that is significantly more effective at the timely recognition of impairment losses on goodwill at a reasonable cost? Why or why not?
- (b) If you do not agree, how should the Board change the impairment test? How would those changes make the test significantly more effective? What cost would be required to implement those changes?
- (c) Paragraph 3.20 discusses two reasons for the concerns that impairment losses on goodwill are not recognised on a timely basis: estimates that are too optimistic; and shielding. In your view, are these the main reasons for those concerns? Are there other main reasons for those concerns?
- (d) Should the Board consider any other aspects of IAS 36 in this project as a result of concerns raised in the Post-implementation Review (PIR) of IFRS 3?

#### Response:

Most committee members agree that it is not feasible to significantly improve the goodwill impairment test at a reasonable cost as there is little or no opportunity to measure goodwill directly.

However, some members are of the view that the IASB could further explore ways to minimize the extent to which impairment tests are based on overly optimistic cash flow projections by management.

Regardless of the different views on the possible improvement of the goodwill impairment test, most members believe there is room for improvement to the proposals for assessing whether more discipline could be provided about the application of the valuation techniques, for example, considering (i) the CGU level of impairment test performed by issuers, (ii) how to deal with cash flow predictions that differ from external evidence, (iii) whether capex support revenues and margin forecasts, (iv) how to assess risks that should be included in the discount rate, and (v) how to estimate terminal value. Further, to reflect the less optimistic scenarios (i.e. downturn) in cash flow predictions, issuers could be required to use a multi scenario model and calculate a weighted average of three (or more) case scenarios – the worst, the base and the best-case scenarios. This is also relevant with regards to terminal value. (Please also refer to our responses on ‘Simplifying the Impairment Test’.) However, some members feel that these points are more compliance issues with the existing requirements. As such, these members believe the Board should consider issuing additional guidance in support of the requirements for more consistent application of the goodwill impairment test.



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We also agree with the Board about concerns regarding the two main reasons for the timely recognition of impairment losses – management over-optimism and shielding.

As for the other aspect of possible enhancement of IAS 36, we believe that there is room for improvement to include disclosure for a so called “close call” situation when no impairment is recognised when an impairment test is conducted. IAS 36.134(f) currently requires an entity to perform sensitivity analysis but we believe an entity should disclose the facts and circumstances with respect to how close it was to impairing goodwill when the entity performed an impairment test. Currently, it is very difficult for users to understand whether an issuer was very close to recognising an impairment or not as a result of an impairment test. In addition, an issuer could mitigate a surprise impairment by providing a “close call” disclosure and giving an early warning to users about the possible impairment in the future. Furthermore, a “close call” case usually becomes an issue with external auditors and it tends to appear as KAMs or CAMs, but there is little information available from the issuer side as to why the goodwill was not impaired. As such, we are of the view that additional disclosure might be needed for a “close call” situation.

#### Question 7

Paragraphs 3.86–3.94 summarise the reasons for the Board’s preliminary view that it should not reintroduce amortisation of goodwill and instead should retain the impairment-only model for the subsequent accounting for goodwill.

- (a) Do you agree that the Board should not reintroduce amortisation of goodwill? Why or why not? (If the Board were to reintroduce amortisation, companies would still need to test whether goodwill is impaired.)
- (b) Has your view on amortisation of goodwill changed since 2004? What new evidence or arguments have emerged since 2004 to make you change your view, or to confirm the view you already had?
- (c) Would reintroducing amortisation resolve the main reasons for the concerns that companies do not recognise impairment losses on goodwill on a timely basis (see Question 6(c))? Why or why not?
- (d) Do you view acquired goodwill as distinct from goodwill subsequently generated internally in the same cash-generating units? Why or why not?
- (e) If amortisation were to be reintroduced, do you think companies would adjust or create new management performance measures to add back the amortisation expense? (Management performance measures are defined in the Exposure Draft General Presentation and Disclosures.) Why or why not? Under the impairment-only model, are companies adding back impairment losses in their management performance measures? Why or why not?
- (f) If you favour reintroducing amortisation of goodwill, how should the useful life of goodwill and its amortisation pattern be determined? In your view how would this contribute to making the information more useful to investors?



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**Response:**

Members have differing views about whether to retain impairment-only or reintroduce amortisation. None of the proposed methods could convince all members and each one has advantages and disadvantages which are discussed in the Discussion Paper.

Those members who favoured reintroducing amortisation of goodwill believe that the impairment test does not seem to be working as effectively as expected (increased or accumulated amount of goodwill, time lags before impairment, significant judgement and subjectivity involved, complexity). These members are of the view that in practice, amortisation provides more objective, understandable information.

These members believe that amortisation of goodwill could relieve some of the pressure that is currently placed on the impairment test, given that the Discussion Paper does not propose options that significantly improve this test. However, those members agree that it is challenging to determine the useful life of goodwill or the pattern in which it is consumed. Having said that, these members also believe that a for-profit acquirer generally has a recovery period in mind for the acquisition price when the pricing of a business combination is negotiated. In any case, they believe that goodwill (or at least significant parts of it, such as workforce or synergies) is not an eternal asset with an infinite lifetime and eventually becomes indistinguishable from subsequently generated value creation. However, many members are concerned that the Board would set up a principles-based approach to estimate the useful life and issuers could end up choosing significantly different useful lives if amortisation is reintroduced. A ‘one-size-fits-all’ lifetime for goodwill does not seem satisfactory and these members would advocate for a principles-based approach with possibly a cap (a maximum period after which goodwill must be completely amortised).

If amortisation were reintroduced, we believe management could determine the amortisation period based on the period over which the acquisition is expected to generate largely independent cash flows or the pay back period (i.e., the period over which management expects to recover the amount paid for goodwill). Either of these approaches would provide more meaningful information to investors.

Allocation of goodwill for impairment testing purposes can impact its subsequent measurement. In practice, under IAS 36, the allocation of goodwill for impairment testing purposes does allow for substantial judgment, especially in larger groups, and there are challenges pertaining to enforcement by auditors and by regulators. How a subsequent impairment will be perceived by the investor community is generally subject to scrutiny within the entities, and may create an incentive for management which can impact both the timing and the amount of such impairment. Although some members argue that determining useful life by management itself could be influenced by management’s incentive, other members are of the view that an amortisation is a predictable or scheduled expense once the useful life is fixed, similar to other depreciation and amortisation expenses, without such incentive.



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These members also believe that there was sufficient feedback on the PIR for IFRS 3 to support the reintroduction of goodwill amortisation. The prohibition of recognising internally generated goodwill is a primary argument in favor of reintroducing amortisation.

On the other hand, those members who favoured retaining the impairment-only model agree with the Board that there is no compelling new evidence at this point to suggest that amortising goodwill would significantly improve the information provided to investors. These members believe that the useful life of goodwill cannot be reliably estimated, so any amortisation expense would be arbitrary and create an irrelevant income statement charge that would likely be removed from the analysis of earnings by investors, and may increase the use of non-GAAP measures (created by analysts, if not created by the company itself in a Alternative/Management Performance Measure) as a result.

Furthermore, based on discussion by some members with investors and other publicly-available information from investors, these members suggest that a change to an amortisation model would be viewed negatively by some/many investors as it would result in a loss of meaningful information in certain situations. While in certain situations impairment may have limited usefulness to investors (largely confirmatory value), some investors have suggested that an impairment model is more meaningful than amortisation, particularly given challenges with determining the appropriate life of goodwill. The recognition of an impairment loss provides important confirmatory information, even if delayed, that confirms investors' earlier assessments that those losses have occurred and holds management to account, especially if the Board were to add "close call" disclosures as suggested above. Finally, these members do not believe that compliance issues associated with application of the existing impairment-only model is either a new or compelling argument for re-introduction of amortisation.

Members that are not in support of the reintroduction of amortisation note that an application of an amortisation model is not costless. There are costs associated with system changes, estimating and monitoring the useful life, plus goodwill would still need to be evaluated for impairment. Further, while some may view the benefits of an impairment model to be somewhat limited, investors consistently say that amortisation does not provide meaningful information. These members believe the IASB should consider these factors in evaluating the costs and benefits from reintroducing an amortisation model.

We believe that acquired goodwill is inherently different from internally-generated goodwill because there is an identifiable transaction with an unrelated party that results in the measurement of acquired goodwill. That being said, we do not believe that acquired (i.e. recognised) goodwill should be separately-identified indefinitely. Our experience is that management often wants to integrate the newly-acquired activities into its existing operations such that over time the newly-acquired business becomes less and less distinct. Therefore, we are supportive of the current approach of assigning goodwill to CGUs (or groups of CGUs) and to re-assigning it when management reorganizes its operations.



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#### Question 8

Paragraphs 3.107–3.114 explain the Board’s preliminary view that it should develop a proposal to require companies to present on their balance sheets the amount of total equity excluding goodwill. The Board would be likely to require companies to present this amount as a free-standing item, not as a subtotal within the structure of the balance sheet (see the Appendix to this Discussion Paper).

- (a) Should the Board develop such a proposal? Why or why not?
- (b) Do you have any comments on how a company should present such an amount?

#### **Response:**

We understand the Board’s view that goodwill is difficult to ascribe to specific cash flow outcomes and that there is a need for disclosure of total equity excluding goodwill so that it could draw investors’ attention to companies whose goodwill constitutes a significant portion of their net assets.

Many members are not fully convinced, however, with the proposal to disclose the total equity excluding goodwill in the company’s primary financial statements. Currently, the Board is proposing that goodwill be presented as a separate line on the statement of financial position in the Exposure Draft for the Primary Financial Statements and these members do not feel adding an additional line item in equity adds value for investors. Instead, these members prefer that this kind of disclosure be presented in the notes. Furthermore, these members are not convinced that this presentation aligns with paragraph 4.63 of the Conceptual Framework where Equity is defined as “the residual interest in the assets of the entity after deducting all its liabilities”. Further, with tagging of data being required in more jurisdictions, investors should more easily be able to manipulate the existing information if such a presentation is important to them.

In addition, the Discussion Paper currently only shows an illustration for a fact pattern with a 100% acquisition. In light of the fact that IFRS 3 provides a transaction-by-transaction policy election on the measurement of NCI, the Board may need to provide further illustrative examples to demonstrate this presentation for less-than-100% acquisitions under both policy elections.

#### Question 9

Paragraphs 4.32–4.34 summarise the Board’s preliminary view that it should develop proposals to remove the requirement to perform a quantitative impairment test every year. A quantitative impairment test would not be required unless there is an indication of impairment. The same proposal would also be developed for intangible assets with indefinite useful lives and intangible assets not yet available for use.

- (a) Should the Board develop such proposals? Why or why not?



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- (b) Would such proposals reduce costs significantly (see paragraphs 4.14–4.21)? If so, please provide examples of the nature and extent of any cost reduction. If the proposals would not reduce costs significantly, please explain why not.
- (c) In your view, would the proposals make the impairment test significantly less robust (see paragraphs 4.22–4.23)? Why or why not?

**Response:**

Members share some degree of concern replacing the annual impairment test with a trigger-based impairment test.

Those members who oppose this believe that the annual impairment test provides a good governance mechanism, prompts management to assess the cash generating processes within its business, and promotes good stewardship. In addition, the disclosures relating to the impairment test are useful, particularly information about the test's assumptions and sensitivities. These members are of the view that removing the requirement for an annual test of goodwill would make impairment tests less robust and would make it harder to prevent the problem of 'too little too late'. However, other members believe the Board should not remove the annual impairment test unless the amortisation of goodwill is reintroduced. If the Board does not reintroduce amortisation, these members believe that a reduction in robustness of the annual impairment test would outweigh any cost savings.

On the other hand, other members support the proposal to remove an annual impairment test because it will reduce the burden for issuers. However, IAS 36.9 will need to be revised so that it is clear that management is responsible to have processes and controls in place to enable it to identify triggers, and the test for impairment would be performed whenever those triggers occur without regard to whether there is a reporting date at hand. Our understanding is that the language in IAS 36.9 results in diversity in practice wherein some entities only evaluate triggers at reporting dates. Entities that do not have interim reporting or that have less frequent interim reporting may have very different impairment outcomes for similar circumstances whereas others may evaluate triggers on an ongoing basis.

Regardless of the different views of members, many members share the view that removal of the annual impairment test could result in challenges in enforcing compliance with the standard. There can be significant judgment in determining whether there has been a trigger, particularly in situations where there is a slow deterioration of the operating performance of a CGU/group of CGUs. In some cases, auditors and securities regulators may not have historically challenged judgments about the existence of a trigger, knowing that there is a required annual impairment test. Removal of the annual test would likely place increased attention on the evaluation of triggers. We believe that if the IASB proceeds down this path, it should consider the need to provide additional guidance on the triggers, or to require an annual impairment test if the expected economic life is over 15 or 20 years.





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Some members suggest asking entities to describe why they conclude that there are no indicators for impairment. It might be helpful if the IASB updates the list of indicators for impairment in IAS 36.12 especially for indicators of impairment of goodwill. We suggest including in the list of indicators that there is a derecognition of goodwill as a result of elements that were not measured at fair value or of contingent assets that are part of the goodwill, when these elements are no longer present and when the contingent asset is realised. Examples include when the goodwill includes an amount that relates to a contingent asset for which the contingency is resolved, or when the goodwill reflects the fact that pension liabilities and deferred taxes are not measured at fair value when the pension liability or deferred taxes are derecognised.

The IASB also may want to consider the use of an annual qualitative (rather than quantitative) test for impairment similar to that used in U.S. GAAP (commonly referred to as “Step Zero”).

Finally, for identifiable intangible assets with indefinite useful lives and intangible assets not yet available for use we suggest maintaining current requirements since it encourages companies to closely track these assets, improving reliability of the recorded amounts.

## Question 10

The Board’s preliminary view is that it should develop proposals:

- to remove the restriction in IAS 36 that prohibits companies from including some cash flows in estimating value in use—cash flows arising from a future uncommitted restructuring, or from improving or enhancing the asset’s performance (see paragraphs 4.35–4.42); and
- to allow companies to use post-tax cash flows and post-tax discount rates in estimating value in use (see paragraphs 4.46–4.52).

The Board expects that these changes would reduce the cost and complexity of impairment tests and provide more useful and understandable information.

(a) Should the Board develop such proposals? Why or why not?

(b) Should the Board propose requiring discipline, in addition to the discipline already required by IAS 36, in estimating the cash flows that are the subject of this question? Why or why not? If so, please describe how this should be done and state whether this should apply to all cash flows included in estimates of value in use, and why.

## Response:

Most members are not in favour of removing the restriction in IAS 36 that prohibits companies from including some cash flows in estimating value in use, primarily because they are not in favour of permitting companies to include uncommitted restructurings or improvements of the asset’s performance. These members believe such removal may exacerbate the problem of impairments being



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recognised ‘too little too late’ since there will be a significant level of judgement involved with estimating what could be identified as an uncommitted restructuring cost.

However, other members support the IASB’s concept of relaxing the restriction prohibiting companies from including some cash flows in estimating value in use – cash flows arising from a future uncommitted restructuring, or from improving or enhancing the asset’s performance. These members believe that the resulting estimate of value in use would incorporate cash flow projections which are regularly prepared, monitored and used internally for decision-making, rather than forecasts produced solely for external financial reporting. However, these members are of the view that the IASB should provide further guidance on when it would be appropriate to include cash flows pertaining to future uncommitted restructurings. In addition, some members believe the Board should consider requiring the disclosure of such uncommitted restructuring plans that was originally considered when calculating the business acquisition price. However, these members also believe that inclusion of uncommitted restructuring plan would not be appropriate if the plan has changed subsequent to the initial price consideration.

Some members share concerns expressed in paragraph 4.40 of the Discussion Paper. These members do not agree with the Board’s preliminary view that there is no need to set a probability threshold or require additional qualitative disclosures in order to avoid overly optimistic assumptions in estimating value in use, although there is a requirement to reflect probability under IAS 36.30(b). Furthermore, these members also feel removing certain of these restrictions on calculating cash flows may result in management making overly optimistic estimations of cash flows. Some members are also concerned with the suggestion in paragraph 4.42 of the Discussion Paper that such a risk of over-optimism can be more effectively addressed by auditors and regulators. Specifically, we often observe over-optimism in the course of our regulatory reviews. However, these occur after financial statements are filed and addressing this over-optimism after the financial statements are already available for investor use does not result in timely information. We are concerned with the rationale discussed in paragraph 4.42 as a basis for the Board’s preliminary view, and as noted above, these members would like to see that the inclusion of cash flows arising from a future restructuring should be clarified by additional guidance or indicators in order to reduce the risk of abusive or inappropriate judgment.

Many members have concern that management’s estimation of value in use may be optimistic and this is very challenging from an enforcement perspective. Some members prefer an approach that would require the recoverable amount to be based on fair value rather than the higher of value in use or fair value less costs to sell. The difference between fair value and value in use (if calculated on the basis of discounted cash flows) results because there are entity-specific cash flows that are not available to market participants. These members understand that, when challenged, management is often unable to support entity-specific cash flows that are significantly greater than market participant estimates are when developing value in use amounts. Because of the guidance that is provided in IFRS 13, these members believe the likelihood of greater consistency in practice is enhanced by using fair value as the recoverable amount rather than attempting to refine the determination of value in use. Further, use of fair value as the recoverable amount makes comparisons to and reconciliations with an entity’s market



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capitalization more meaningful and useful as evidence about the application of the impairment test. Also, use of fair value may enhance the prospects of convergence with U.S. GAAP.

We support allowing companies to use post-tax cash flows and post-tax discounting rates when estimating the value in use. Post-tax discount rates are easier to determine because they often are observable and their use could reduce the cost and effort to project the value in use. We also consider the IASB should try to standardise the treatment of discount rates across its standards, since the current diversity creates confusion among IFRS users and generates unnecessary costs.

However, some members consider that it may be necessary that the Board address the circumstances when a deferred tax liability related to the recognition of assets in a business combination is part of the carrying amount of the CGU. This issue is related to the day one impairment of goodwill due to the recognition of deferred tax liabilities (DTLs). To avoid this impairment charge, the professional literature suggests deducting DTLs when determining the carrying amount of the CGU's net assets. However, the guidance provided by IAS 36 is very limited in this regard resulting in diversity in practice and enforcement challenges.

#### **Question 11**

Paragraph 4.56 summarises the Board's preliminary view that it should not further simplify the impairment test.

- (a) Should the Board develop any of the simplifications summarised in paragraph 4.55? If so, which simplifications and why? If not, why not?
- (b) Can you suggest other ways of reducing the cost and complexity of performing the impairment test for goodwill, without making the information provided less useful to investors?

#### **Response:**

We generally agree with the IASB's proposal in Paragraph 4.56 in the Discussion Paper to not further simplify the impairment test.

We consider it would be very useful if the standard itself provided more guidance on the allocation of goodwill to CGUs. In practice we have seen some entities allocating goodwill to very large CGUs/Groups of CGUs; sometimes entire segments are defined as CGUs/Groups of CGUs and it is very difficult to assess whether the goodwill will effectively contribute to the entire segment to which it was allocated.

However, some members do not support the tentative decision made by the Board to not provide more guidance on the difference between entity-specific inputs used in value in use and market-participant



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inputs used in fair value less costs of disposal. These members think that the guidance provided by IAS 36 in this regard is very limited and should be enhanced.

#### **Question 12**

Paragraphs 5.4–5.27 explain the Board’s preliminary view that it should not develop a proposal to allow some intangible assets to be included in goodwill.

- (a) Do you agree that the Board should not develop such a proposal? Why or why not?
- (b) If you do not agree, which of the approaches discussed in paragraph 5.18 should the Board pursue, and why? Would such a change mean that investors would no longer receive useful information? Why or why not? How would this reduce complexity and reduce costs? Which costs would be reduced?
- (c) Would your view change if amortisation of goodwill were to be reintroduced? Why or why not?

#### **Response:**

We support the Board’s view not to develop a proposal to allow some intangible assets to be included in goodwill. We think that the recognition of intangibles assets separately from goodwill provides useful information.

As the useful life of identifiable intangible assets cannot be presumed to be the same as the useful life of an unidentifiable intangible asset, our answer would not change even if amortisation of goodwill were to be reintroduced.

#### **Question 13**

IFRS 3 is converged in many respects with US generally accepted accounting principles (US GAAP). For example, in accordance with both IFRS 3 and US GAAP for public companies, companies do not amortise goodwill. Paragraphs 6.2–6.13 summarise an Invitation to Comment issued by the US Financial Accounting Standards Board (FASB).

Do your answers to any of the questions in this Discussion Paper depend on whether the outcome is consistent with US GAAP as it exists today, or as it may be after the FASB’s current work? If so, which answers would change and why?



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**Response:**

IOSCO strongly supports the objective of a single set of high-quality accounting standards that are consistently and rigorously applied. This view is also shared by the leaders of G20 and other international organizations.<sup>3</sup> With this in mind, many members encourage the IASB to work closely with the FASB so that convergence with U.S. GAAP in this area can be maintained or perhaps even enhanced. We believe that the final IASB requirements should not lead to a different accounting treatment related to goodwill under IFRS and U.S. GAAP in order to ensure the greatest degree of comparability as possible for financial statements prepared under IFRS and U.S. GAAP. In our experience, the likelihood of achieving a converged outcome is greatly enhanced when the two Boards are working collaboratively, including similar timelines with their respective projects. We believe that maintaining convergence with U.S. GAAP on this topic should continue to be an important consideration.

**Question 14**

Do you have any other comments on the Board's preliminary views presented in this Discussion Paper? Should the Board consider any other topics in response to the PIR of IFRS 3?

**Response:**

We do not have further comment.

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We appreciate your thoughtful consideration of the views provided in this letter.

If you have any questions or need additional information, please do not hesitate to contact Cameron McInnis, Chair of the Accounting Subcommittee of Committee 1 at +1 416-593-3675 or myself. In case of any written communication, please mark a copy to me.

Yours sincerely,

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<sup>3</sup> Why global accounting standards? <https://www.ifrs.org/use-around-the-world/why-global-accounting-standards/>



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Makoto Sonoda

Chair  
Committee on Issuer, Accounting, Audit and Disclosure  
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