This paper has been prepared by the EFRAG Secretariat for discussion at a public meeting of EFRAG TEG. The paper forms part of an early stage of the development of a potential EFRAG position. Consequently, the paper does not represent the official views of EFRAG or any individual member of the EFRAG Board or EFRAG TEG. The paper is made available to enable the public to follow the discussions in the meeting. Tentative decisions are made in public and reported in the EFRAG Update. EFRAG positions, as approved by the EFRAG Board, are published as comment letters, discussion or position papers, or in any other form considered appropriate in the circumstances.

Summary and analysis of the comment letters received

1 Based on the comments received, the EFRAG Secretariat has developed a revised draft EFRAG final comment letter that is presented as agenda paper 01-05.

Structure of the paper

2 This comment letter analysis contains:

(a) Background;

(b) Summary of respondents;

(c) Summary of respondents' views;

(d) Appendix 1 - detailed analysis of responses to questions in EFRAG's draft comment letter and questions to EFRAG TEG; and

(e) Appendix 2 – list of respondents.

Background

3 The IASB issued it Discussion Paper 2020/1 *Business Combinations—Disclosures, Goodwill and Impairment* on 19 March 2020 (the 'DP'). The objective of the DP is to explore whether companies can, at a reasonable cost, provide investors with more useful information about the acquisitions those companies make.

4 The DP considers the following topics identified in the PIR of IFRS 3:

(a) disclosing information about acquisitions;

(b) testing goodwill for impairment—effectiveness and cost;

(c) whether to reintroduce amortisation of goodwill; and

(d) recognising intangible assets separately from goodwill.

5 On 29 May 2020, EFRAG has published its draft comment letter in response to the IASB's DP 2020/1 Business Combinations—Disclosures, Goodwill and Impairment and seeks constituents' views on the proposals. In its draft comment letter EFRAG supported the objective to explore whether companies can, at a reasonable cost, provide investors with more useful information about the acquisitions companies make.

6 The DP proposed to require information about the strategic rationale and management's objectives for an acquisition as at the acquisition date and subsequent disclosures about whether an acquisition is meeting those objectives. The DP also proposed information about synergies which EFRAG acknowledged would be useful. However, EFRAG noted some practical issues to consider in relation to such disclosures and sought constituents' views on whether this information should rather be in the management commentary rather than the financial statements. EFRAG also questioned whether the benefits of some of the disclosures would outweigh the costs.

7 The DP stated that it is not possible to make the impairment test for cash-generating units containing goodwill significantly more effective. EFRAG suggested that the guidance on goodwill allocation to cash generating units is considered by the IASB and possibly amended to improve how the test is applied in practice. In addition, better disclosures of estimates used to measure recoverable amounts of cash-generating units containing goodwill could be considered. EFRAG sought constituents' views on possible disclosure proposals to mitigate the risk of management over-optimism.

8 The DP suggested that amortisation of goodwill should not be reintroduced. In the draft comment letter EFRAG did not form a view on this issue and sought inputs from its constituents on new evidence, new arguments or new assessment on the existing evidence to support a change.

9 EFRAG appreciated the IASB's attempts to simplify the impairment test. However, EFRAG had reservations about introducing an indicator-only approach. EFRAG supported the IASB's proposal to remove the restriction in IAS 36 Impairment of Assets that prohibits companies from including cash flows arising from a future uncommitted restructuring or from enhancing the asset's performance as well as to remove the requirement to use pre-tax inputs and pre-tax discount rates to calculate value in use.

10 EFRAG did not assess that there would be any benefits of presenting the amount of total equity excluding goodwill in the statement of the financial position. Finally, EFRAG would recommend that the issue on whether some intangible assets could be included in goodwill should be considered in a second phase of the project following a revision of IAS 38 Intangible Assets.

Summary of respondents

11 At the time of writing, nine comment letters and uploaded as well as 12 draft comment letters have been received. Further information about the respondents can be found in appendix 2. The letters are summarised below by type of respondent for questions where the type of respondent seem to determine the response. Where this is not the case, the letters are summarised by the views provided.

Summary of respondents' views

Question 1: Meeting the objectives of the project

12 Preparers generally did not see the proposals as a package and whether the proposals meet the project objective. Some users also did not see the proposals as a package. One of the users noted the disclosures alone are insufficient to address concerns about delayed goodwill impairment and some of their members consider the goodwill amortisation should be included in the package.

13 Auditors were supportive of the DP's objective as it will improve investors' understanding and make management more accountable for these decisions. They only partially supported the preliminary views had several reservations. Similarly, standard setters and regulators supported the objective but had several comments.

Question 2: New disclosure requirements

Disclosure requirements resolve the issue[1]

14 Almost all preparers opposed, had concerns with the proposed disclosures or asked to review the usefulness of the current disclosures first. One preparer agreed to disclose information about the primary reasons and business rationale for an

[1] Some sub-questions were only answered by a few participants.

acquisition. In contrast, users supported the proposed improving disclosures. For investors it is fundamental that companies provide useful information to (1) accurately analyse the value of the acquisition, (2) the resulting value of the entity and (3) to understand the amount of the recognised goodwill.

15 Messages from standard setters were mixed. Some standard setters noted that the proposed disclosures are of limited use. Others thought the disclosures would be useful. Two standard setters argued from a different angle. While agreeing to or welcoming the objective of the disclosures, they either encouraged the IASB to perform extensive field testing, reach out to stakeholders and then significantly reconsider its proposals or suggested substantiating, amending and clarifying the disclosure objective.

16 Auditors and regulators agreed with enhancing the information provided to investors about the subsequent performance of an acquisition.

Strategic rationale and management's (the chief operating decision maker's (CODM's)) objectives

17 One preparer supported the disclosure about the primary reasons and management' strategic rationale for the business combination at the acquisition date. Users also agreed with this. Auditors and regulators also expressed support.

18 Most standard setters generally agreed with the requirements to disclose providing the strategic rationale for undertaking an acquisition and management's objectives for the acquisition.

(Not) monitoring the acquisition – stop monitoring – change metrics

19 One preparer noted that the requirement to state why the entity does not monitor an acquisition seems to us to be an attempt to force entities to disclose the metrics it uses by the method of "naming and shaming". In the view of the participant an entity should be allowed to state that it is monitoring the acquisition but that for reasons of confidentiality and commercial sensitivity it chooses not to disclose the metrics.

20 One standard setter agreed with the proposal to disclose how management (CODM) monitors and measures the acquisition is at an appropriate level of details. The metrics disclosed will give investors relevant information about how management monitors and follow up an acquisition and about how well a company is managed. With regards to quantitative disclosure requirement on such metrics the Board should emphasise that only metrics that can be measured (and audited) with sufficient reliability should be within the scope for quantitative disclosures.

21 Users thought that specific information will provide a better base for understanding and valuing the entity. Hence, companies should provide metrics that are relevant for investors such as estimates of consolidated revenues, operating profits, cost savings, net earnings and balance sheet items such as consolidated debt and ROCE. Other type of non-financial information such as (combined) market share and/or other information (e.g., number of retail stores if that is the case) would also be helpful. Users agreed with EFRAG's comments regarding the subsequent monitoring of the performance of an acquisition. They dissent with the DP's argument that an entity cannot provide information because the acquired business is integrated.

22 In the view of a regulator a company should stop providing disclosures about whether it is meeting its objectives only when the synergies expected to derive from the acquisition have been realised or when those objectives have been abandoned (which in their view corresponds to the time when an acquired business is fully integrated into the acquiring business).

Based upon CODM reviews

23 Some preparers noted that if the disclosures would be required, they should be based on the information and the acquisitions a company's CODM reviews. Other preparers asked the IASB to perform further field tests to obtain further evidence on whether these proposals would work in practice or noted the information should remain rather qualitative and materiality criteria should be considered.

24 Two standard setters suggested to consider a lower management level – at least in some cases - as the threshold for monitoring the acquisitions (e.g., the level at which goodwill is being monitored internally) and disclose metrics used by this lower management. One standard setter emphasized that such disclosures should be built on management's metrics provided to the CODM for relevance and cost/benefit trade-off reasons. Another one supported the CODM approach for pragmatic reasons and due to the lack of a superior, sufficiently objectifiable alternative, even though not every significant transaction is likely to be reported at the CODM level.

25 In the regulators' view at least some key disclosures should be required for all the acquisitions which generate a material amount of goodwill, regardless of whether they are monitored by the CODM.

Commercial sensitivity

26 All preparers had concerns with relation to commercial sensitivity of the information, just like most of the standard setters.

27 In contrast, users noted to understand that companies cannot provide commercially sensitive information but note that companies under the caption of "sensitiveness" in many cases do not provide information that in fact is not that sensitive. They agreed with EFRAG's comments that a balance should be reached.

28 Also, auditors suggested the IASB to consider the right balance between the benefits to investors and the commercially sensitivity of these disclosures. A regulator thought that generally commercial sensitivity is not a valid reason for not informing investors.

Forward-looking nature of the information

29 Only a few participants (preparer, standard setters) opined that information established or generated at the time of the acquisition is forward-looking by nature, even though it was determined in the past. The quantified expected outcomes from an acquisition are necessarily projections into the future of what management expects from the transaction in terms of profitability, etc. Consequently, the IASB must accept that this information is of the nature of a projection into the future.

30 One standard setter pointed out that a valid statement of objectives may also require a plausible presentation of the expected way of achieving these objectives. Therefore, they deemed a legal assessment difficult, whether information about management´s objectives for an acquisition along together with detailed targets could be considered as forward-looking information. In order to find a universally applicable suitable solution, the IASB might consider whether information classified as forward-looking in a particular jurisdiction should not be subject to mandatory disclosure for companies in that jurisdiction.

Notes to the financial statements vs management commentary

31 Almost all preparers were not in favour of including this information in the notes of the financial statements – but should be provided in the management commentary instead - from a cost/benefit perspective as they do not share the view that it would be more useful, relevant or reliable if audited. One of them noting that putting the information in the management commentary would not make such a big difference.

32 Users noted that currently, information about the business strategy is included in the management commentary. They added that reliability and auditability of the information in M&As should not depend on the circumstances. As the process of consolidation develops new or different information might appear but the information disclosed should be reliable.

More useful if audited / possible to audit

33 One preparer noted that many acquisitions are based on cost synergies. However, tracking these cost savings along the subsequent periods after the acquisitions for the purpose of a disclosure may be difficult, unreliable and thus irrelevant for the users.

34 Most standard setters noted the information is difficult to audit or creates auditability issues. One of them thought that the verifiability of the information supporting the proposed disclosures is a real practical issue. Many of the metrics the CODM uses may be non-financial (such as market shares) and, if having a financial nature, may not be defined by IFRS Standards. In addition, part of the information an entity would disclose would reflect management's expectation and thus, be forward-looking in nature.

35 Some standard setters noted the information provided by the companies will be more useful or relevant and/or reliable if it is audited. One standard setter thought it would be possible to prepare the information in a manner that would make it possible to audit.

Constraints

36 Only one standard setter noted the existence of some existing constraints. Three others were not aware of any constraints which prevent an entity in their jurisdiction to disclose the information proposed in the DP.

Question 3: Helping investors understand expected benefits of and the extent to which an acquisition is meeting CODM objectives

37 Almost all preparers agreed with the usefulness of providing this information to investors but almost all of them also raised concerns at the same time.

38 Also, several national standard setters considered the information to be useful. Two of them agreed in principle with broadening the existing disclosure requirements but asked first to seek feedback on disclosure objectives or to better substantiate them.

39 Regulators agreed with the IASB preliminary view that it should develop, in addition to the proposed new disclosure requirement, proposals to add disclosure objectives to provide information to help investors to understand the benefits a company's management expects from an acquisition and the extent to which an acquisition is meeting the CODM's objectives.

Question 4: Disclosures about synergies and additional major classes of liabilities

40 While almost all the respondents recognised that information on synergies underlying the proposed disclosures provides investors with useful information, many of them were against producing the information requested under a quantitative perspective. Furthermore, almost all the preparers believed that similar information is already provided to investors in the management commentary and in other communication to investors outside the financial statements.

41 Some of the respondents suggested that further clarifications and guidance on the concept of synergy, including how it should be estimated, would increase comparability of the disclosures between companies.

42 A significant portion of the preparers and standard setters considered the proposed disclosures on synergies to trigger commercial sensitivity issue. The same input has been also provided by an auditor.

43 Almost all the preparers and the standard setters providing specific input on this issue considered that the management commentary was the most appropriate placement for this disclosure.

44 Users were divided. One of them noted that users would like to know in a quantifiable manner what are the synergies and estimated contribution to results of the combined business. Another one considered that synergies are seldom hard numbers and an excessive focus on short-term savings can cause long-term damage. It noted that is important that the IASB would not unintentionally create an environment where management will focus on hitting short-term synergy targets at the expense of longer-term stewardship, as bad drafted standards could lead to undesirable management behaviour.

45 Auditors and almost all standard setters considered that the disclosures on expected synergies would provide useful information to investors to better understand the potential impact of an acquisition on the combined financial statements of an entity.

46 Apart from few instances, the majority of respondents agreed to specify that liabilities arising from financing activities and defined benefit pension liabilities are major classes of liabilities.

Question 5: Provision of pro forma information – disclosing revenue and profit or loss of the acquired business post acquisition date – replacing profit or loss with operating profit before acquisition related transaction and integration costs

47 Preparers had different views. Some wanted to retain the IFRS 3 information. Some do not support the proposal to provide information related to the acquired business after the acquisition date or disagree with retaining the pro forma information.

48 Users stated that the current proforma disclosures are almost universally unsatisfactory and that the standard should focus on providing companies with robust guidance rather than being overly prescriptive.

49 Auditors were concerned that with IFRS 3 the proposals will lead to boilerplate and costly disclosures but supports more guidance to be issued by the IASB on the preparation of such information. Consistency and auditability would be improved if the IASB requires the disclosure of the basis of preparation.

50 Most standard setters were in favour to keep the IFRS 3 information but added various comments on expanding it. One regulator warned that the term proforma information could be confusing as this term is used in the context of prospectuses.

Question 6: Designing a more effective impairment test

51 Almost all of the respondents agreed that it would not be feasible to design a significantly more effective impairment test at a reasonable cost. Also, a majority of the respondents agreed that too optimistic estimates and 'shielding effect' were the main reasons for not recognising impairment losses on goodwill on a timely basis. Those who disagreed tend to consider that too late recognition of impairments is not a widespread issue and that management over-optimism is not a cause for such an issue.

52 A slight majority of respondents did not share the IASB's views that management over-optimism should be addressed by auditors and regulators

53 In relation to the suggestions made to improve the impairment test, the views provided differ mainly between preparers and other respondents like users, auditors

and standard setters or regulators. While preparers are mainly reluctant to improve the guidance on allocation or reallocation of goodwill or to consider additional disclosures to make management overoptimism more transparent such proposals were appreciated by other groups of respondents.

54 Improvement of guidance on allocation or reallocation of goodwill to CGUs was more widely supported by respondents that considering additional disclosures. Those in favour of additional disclosures suggested that the IASB would explore additional disclosures on assumptions considered in cash flow estimates.

Question 7: Amortisation of goodwill

55 A majority of respondents representing national standard setters, preparers and users were in favour of reintroduction of goodwill amortisation. These respondents were of view that impairment model was not working as intended and cannot be improved at a reasonable cost and therefore amortisation was a practical solution. From conceptual point of view, they considered goodwill to be a wasting asset which should be amortised to reflect its consumption.

56 Few respondents were in favour of keeping the existing impairment model on the grounds that the impairment test was the only conceptually correct model, that problems lied within its application and that it provided relevant and useful information to users and investors. These respondents also considered that no new arguments were provided to justify a change. In their view the impairment model worked as intended and no significant facts or circumstances were identified that would lead to reconsider the conceptual argument.

57 Some respondents representing preparers', professional organisations, and national standard setter, did not express a view, mentioning that both approaches had their advantages and disadvantages and absence of the new compelling evidence to support one of them.

58 Some respondents considered that management could estimate the useful life based on a goodwill consumption pattern, the payback period of the investment and the amortisation pattern - on the basis of the realisation of the expected synergies.

59 Only one respondent considered disclosing the age of goodwill useful as it would provide relevant information to users. Another one did not agree because it would simply be misleading, where useful lives cannot be determined.

Question 8: Presenting amount of total equity excluding goodwill on the balance sheet

60 Almost all respondents did not support the IASB's proposal to require companies to present on their balance sheets the amount of total equity excluding goodwill. Some of the arguments used were:

(a) this would contradict the recognition of goodwill as an asset.

(b) the figure can be computed easily, and

(c) the IASB's proposal would be more harmful and misleading than beneficial

61 One respondent supported the proposal as they agreed with the IASB rationale that it is essential to make even more transparent the unique nature of the goodwill asset as a residual item. It would be also in line with the prudence principle.

62 Users had mixed views as some members consider that this disclosure would not benefit users as it re-classifies goodwill as an artificially created intangible and the metric can be recalculated easily. Others considered that the disclosure would display the quality of capital to users and act as a bulwark against the delayed recognition of impairment.

Question 9: Removal of quantitative impairment test every year

63 The majority of the respondents, represented mostly by auditors and national standard setters, do not support the indicator-only approach because it reduces the robustness of the test, increases management judgment and does not reduce cost. The majority of the respondents who do not support the indicator-only approach would do so if amortisation of goodwill was reintroduced. Some of the respondents suggest enhancing the current relief in paragraph 99 of IAS 36 Impairment of Assets as an alternative to the indicator-only approach.

64 The respondents in favour of the indicator-only approach, represented mostly by preparers and user, argue that the quantitative impairment test does not add value when significant headroom is available. Some respondents also request additional guidance on the identification and use of indicators if the indicator-only approach is introduced. Users were mentioning that a robust and justifiable catalogue of triggering events is necessary.

Question 10: Remove restriction including some cash flows in estimating value in use-allow to use post-tax cash flows and post-tax discount rates in estimating value in use

65 Most of the respondents support the removal of the restriction to include cash flows from future uncommitted restructurings and asset enhancements in the VIU calculation as it aligns the input used with available management information reducing cost and complexity. Many respondents request additional guidance to clarify which cash flows can be included and to determine a threshold. Some respondents who do not support this simplification argue that the subjectivity and over-optimism is even further increased, in particular for uncommitted future restructurings as it lacks documentation.

66 Almost all respondents support the use of post-tax input in the VIU calculation as it removes the artificial determination of pre-tax inputs making it less complex and less costly. Some respondents require additional guidance on alignment with IAS 12 Income Taxes regarding the impact of deferred tax assets from carrying forward tax losses.

Question 11: No further simplification of impairment test

67 Many respondents support the IASB's preliminary view that no further simplifications need to be developed and are in particular opposed against using a single method for the recoverable amount. Other simplifications suggested by respondents:

(a) Some respondents request further guidance on allocation of goodwill to CGUs as it would improve the effectiveness of the impairment test;

(b) Few respondents request further guidance on determining the discount rate, referring to the educational material for IFRS 13 (2013) as an example of useful guidance;

(c) Few respondents request further guidance on including the carrying amount of lease liabilities and cash outflows relating to lease instalments under IFRS 16 Leases when calculating the VIU, to avoid divergence in practice; and

(d) Few respondents request further guidance requiring separate recognition of technical goodwill relating to deferred tax liabilities as the use of this technical goodwill is directly related to the settlement of the related deferred tax liability and should not be shielded.

Question 12: Not including some intangible assets in goodwill

68 The majority of the respondents support the proposal to not develop requirements to add intangible assets acquired in a business combination to the carrying amount of goodwill. The main argument is that it provides useful information to users regarding the consideration paid for the acquisition and in line with the increasing

importance of intangibles in contemporary economies. Nonetheless, most of the respondents acknowledge the challenges relating to the subjectivity and complexity of valuation, however these can be overcome. Many respondents support a dedicated and comprehensive review project on IAS 38 Intangible Assets, but some respondents urge for a narrow-scoped review on short-term relating to intangible assets acquired in a business combination.

Question 13: Convergence with US GAAP

69 Almost all respondents support convergence with the FASB and in general emphasise that it should not be the main goal. Many respondents request that the IASB ensures convergence with the FASB's position on disclosure of subsequent performance of acquisitions as divergence may result in competitive disadvantage for companies that comply with IFRS Standards. Many other respondents request that the IASB ensures convergence with the FASB's position on subsequent accounting for goodwill.

Question 14: Any other comments

70 Comments raised varied. Some examples:

(a) One preparer organisation disagreed with the view that management will be held (more) accountable when making a corporate operation by way of disclosures. This especially because of the exaggerated influence given to disclosures in the financial statements when, at present, there are other mechanisms to verify the performance of a company and its top management.

(b) A user organisation recommended separate disclosure of internally generated assets and those marked-up during an acquisition. The disclosure would enable users to obtain a better view of overall operating performance.

(c) One respondent considered that the issue around deferred tax liabilities and goodwill is best addressed by the reintroduction of the amortisation of goodwill. Another respondent did not support changing the current accounting for goodwill relating to the deferred taxes mismatch. On reversals of the impairment of goodwill, they do not support the introduction of reversals of goodwill impairment.

(d) One respondent recommended that the IASB provides further guidance where the business combination involve the acquisition of an entity with one, or only a few, assets with the tax base significantly lower than the related fair value(s).

Question to EFRAG TEG

71 Does EFRAG TEG have questions on the EFRAG Secretariat's summary in *Appendix 1: Analysis and Summary of Comments* received?

Appendix 1 - Detailed analysis of responses to questions in EFRAG's draft comment letter

Table of contents page

Question	page
Question 1	11
Question 2	15
Question 3	32
Question 4	35
Question 5	42
Question 6	46
Question 7	56
Question 8	64
Question 9	66
Question 10	70
Question 11	74
Question 12	77
Question 13	82
Question 14	84

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?

Proposals in the DP

72 *The IASB's overall objective is to explore whether companies can, at a reasonable cost, provide investors with more useful information about the acquisitions those companies make. Better information would help investors assess the performance of companies that have made acquisitions. Better information would also be expected to help investors more effectively hold a company's management accountable for management's decisions to acquire those businesses.*

73 *The IASB's preliminary views are that it:*

(a) *should develop proposals to enhance the disclosure objectives and requirements in IFRS 3 Business Combinations to improve the information provided to investors about an acquisition and its subsequent performance (Section 2);*

(b) *cannot design a different impairment test for cash-generating units containing goodwill that is significantly more effective than the impairment test in IAS 36 at recognising impairment losses on goodwill on a timely basis and at a reasonable cost (Section 3);*

(c) *should not reintroduce amortisation of goodwill (Section 3);*

(d) *should develop a proposal to help investors better understand companies' financial positions by requiring companies to present on their balance sheets the amount of total equity excluding goodwill (Section 3);*

(e) *should develop proposals intended to reduce the cost and complexity of performing the impairment test by:*

   (i) *providing companies with relief from having to perform an annual quantitative impairment test for cash-generating units containing goodwill if there is no indication that an impairment may have occurred; and*

   (ii) *extending the same relief to companies for intangible assets with indefinite useful lives and intangible assets not yet available for use (Section 4);*

(f) *should develop proposals intended to reduce cost and complexity, and to provide more useful and understandable information by simplifying the requirements for estimating value in use by:*

   (i) *removing the restriction on including cash flows from a future uncommitted restructuring or from improving or enhancing an asset's performance (Section 4);*

   (ii) *permitting the use of post-tax cash flows and post-tax discount rates (Section 4); and*

   (iii) *not changing the range of identifiable intangible assets recognised separately from goodwill in an acquisition (Section 5).*

74 The IASB's preliminary views set out in the Discussion Paper form a package and are interconnected. The IASB considered the links when considering the package and whether it would meet the project's objective. The IASB asks that when stakeholders assess what best meets the project's objective, they also consider these links.

75 In reaching its preliminary views, the IASB considered the expected benefits and expected costs of the overall package. In the IASB's view this package of preliminary views is the most cost-effective response to the range of views expressed by stakeholders in the PIR of IFRS 3 about investor needs, benefits and costs in accounting for acquisitions and goodwill.

EFRAG's tentative position

EFRAG supports the objective of the DP to explore whether companies can, at a reasonable cost, provide investors with more useful information about the acquisitions those companies make. It is our understanding that users of financial statements do not think that sufficient information to assess acquisitions is currently presented in financial statements. It is therefore important to address this issue.

EFRAG notes that the proposals in the DP do not aim at addressing, through disclosure or enhancement of the impairment model, shortcomings in goodwill accounting. Accordingly, the proposals would address some current shortcomings, but would leave room for improvement in this area.

[As EFRAG is seeking views from its constituents on some of the proposals included in the DP, an answer to the question on whether the proposals in the DP, as a package, meet the objectives of the DP, will only be provided after receiving this input.]

Summary of constituents' comments

76 Respondents to the draft comment letter had a range of views.

Preparers

77 One respondent agrees with some of the IASB's views in paragraph IN9, but not all and so consider that the package would not meet the project objective. They also consider that the proposals have limited inter-relationships and see the DP as a list of largely independent proposals which is echoed in the response. The respondent queried whether the costs of the additional disclosures would be offset by the reduced cost from simplified impairment testing which has targeted and narrow improvements. In response to question 9, the respondent makes it clear that it would continue to perform the quantitative impairment testing for internal purposes. As a whole, the benefits of the package will not demonstrably exceed the costs.

78 One preparer organisation agrees with the overall objective as described in the IASB's DP but have concerns about the proposed disclosures of post-acquisition objectives including targets may be commercially sensitive. Furthermore, it may result in a disproportionate volume of disclosures which may not be coherent and

concise and therefore, not useful. The same applies about disclosures whether an acquisition meets its objectives. They support proposals to reduce cost and complexity of performing impairment tests, but do not agree with the disclosure proposal of equity before goodwill as this is inconsistent with the nature of goodwill as an asset.

79 Another preparer organisation disagrees that the DP represents a package, and that the simplification of the current impairment test comes at the price of increased disclosures about acquisitions. They agree with the simplifications and the related cost savings but consider these insufficient in the context of the additional costs and the commercial sensitivity of the proposals.

80 An insurance preparer organisation also disagrees that the proposals meet the project objective as the DP focuses on additional disclosures whereas the concerns relating to the measurement of goodwill is unaddressed. The respondent is concerned that sudden write-offs would have pro-cyclical effects which would cause concern from a financial stability perspective. The respondent considers that an accounting policy choice for the subsequent accounting of goodwill is the best way to address the concerns.

81 Another preparer organisation disagrees that the proposals are a package and considers that the simplifications relating to impairment testing should be implemented as quickly as possible. However, the proposals around additional disclosures are considered to be significantly damaging to European stakeholders that it could only be considered if only accepted in US GAAP. It also considers that IFRS should not place more stringent requirements than those of US GAAP.

Users

82 One respondent considers it appropriate that the IASB has undertaken this project but considers the DP not as a package, but that the issues can be analysed independently.

83 Another user organisation agrees that acquisition disclosures are unsatisfactory, and needs improving and so welcomes the IASB's project which may overlap with the management commentary project. However, the disclosures alone are insufficient to address concerns about delayed goodwill impairment and some of their members (but not a majority) consider the goodwill amortisation should be included in the package. Debating the process of testing goodwill for impairment is their view asking the wrong question. As the DP states, goodwill cannot be directly measured; it is simply the gap between the consideration paid and the measurable net assets received on consolidation. Testing goodwill for impairment will therefore never be anything other than a subjective exercise. In their comment letter they listed topics users want more information about.

Auditors

84 One respondent supports the DP's objective as it will improve investors' understanding and make management more accountable for these decisions. However, they only partially support the preliminary views in paragraph IN9 and have the following reservations:

(a) The CODM may not be the correct threshold for the proposed disclosures;

(b) The disclosures should be allowed by cross reference in the management commentary or in the notes to the financial statements;

(c) More guidance is needed on synergies disclosures as well as the preparation of proforma information;

(d) They do not have a preference between amortisation or impairment-only model for subsequent accounting of goodwill;

(e) They do not support the proposal to present 'total equity excluding goodwill' in the balance sheet; and

(f) They do not support an indicator-only approach.

Standard setters and regulators

85 One respondent supports the DP's objective but considers that more needs to be done around subsequent accounting for goodwill.

86 Another respondent also agrees with the objective, but do not support certain preliminary views of the IASB:

(a) Concerned about the commercial sensitivity of some of the proposed disclosures

(b) Level of information to be disclosed should be based on that provided to a lower level of management than the CODM and the related metrics

(c) Over-optimism cannot be corrected by auditors and regulators due to the information asymmetry as they cannot make enforceable corrections to a business plan beyond technical or obvious mistakes

(d) Favouring the return of amortisation

(e) Disagrees in respect of total equity excluding goodwill and indicator-only approach.

87 One respondent agrees with the overall objective of the project but is not convinced that all the matters in the DP are interrelated. For instance, the respondent does not agree that the accounting for goodwill and the simplification of the impairment test depend on the information about the subsequent performance of an acquisition. An impairment test may provide some information about the failure of an acquisition, but not necessarily whether it meets the objectives set at the acquisition date. Accordingly, the respondent does not consider the DP as a single package but rather two separate sets – one about disclosures and another about the subsequent accounting for goodwill with costs being the only discernible link. At this stage it is not possible to conclude about costs given the early stage of the project as well as the significant concerns about some of the proposals.

88 Another respondent agrees with the overall objective and that the objective may be fulfilled by the proposed disclosures. The respondent considers that the disclosures can be provided at a reasonable cost given the flexibility of the proposals by focussing on information provided to the CODM.

89 A respondent considers that the proposals do not necessarily need to be judged as a package. Whereas another standard setter does not agree that the package would meet the objective of the project. While respondent agrees that the effectiveness of the impairment test cannot be significantly improved, it considers that the criticism of too little too late against impairment recognition has hardly been addressed. It also considers that goodwill amortisation should be further investigated by the IASB. The commercial sensitivity of information to be disclosed may be a significant hurdle to overcome and the respondent considers that the IASB is over-optimistic about what information is internally available. The respondent also points out that the IASB assertion that the proposed disclosure are objectives to be met rather than forecasts should be assessed from a legal perspective.

90 Another respondent agrees with the overall objective but is of the view that the IASB needs to investigate information currently prepared and monitored by the CODM in this area including field tests with both users and preparers. This answer depends on the answers to the indicator-only approach and other simplifications as well as the reintroduction of the amortisation of goodwill.

91 Another respondent agrees that the DP respond to its overall objective. However, they are concerned about the fact that the DP is too focused on the disclosures and it does not sufficiently address the issue related to the application of the impairment test. This is confirmed by the DP that states that the preliminary view on disclosures is central to its package of preliminary views. Lastly, they consider that the DP discusses only superficially separating goodwill into components and does not consider the guidance about the allocation/reallocation of the goodwill to the CGU(s).

92 Another respondent considers that the objective is important, specifically with reference to improving information provided about an acquisition and its subsequent performance, separately from other proposals. The respondent also considers the proposals do not address the issue around goodwill impairment being recognised too little too late and that the impairment model can be improved. It also deems the re-introduction of the amortisation of goodwill a consequence if the impairment test cannot be improved and would also only support an indicator-only approach in such a case.

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).

(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?

Proposals in the DP

93 *The DP proposes that:*

(a) *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.*

The DP notes that IFRS 3 requires a company to disclose the primary reasons for an acquisition. This disclosure requirement may result in companies providing some information about management's objectives, but, according to the DP, this information is unlikely to be specific enough to form the basis of the information that would help investors to assess the subsequent performance of the acquisition.

(b) *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, rather than on metrics prescribed by the IASB.*

According to the DP, management's objectives, being the objectives of the acquisition that management considers must be achieved for the acquisition to be a success, would form the basis of the information to help investors assess the subsequent performance of the acquisition.

Investors would be able to use the information to assess whether the price for the acquired business appears reasonable.

The preliminary view expressed in the DP would require companies to disclose information management uses to monitor the subsequent performance of an acquisition. If management plans to integrate an acquired business, it is possible that management plans to monitor the subsequent performance of the acquisition using information about the combined business. Companies would be required to disclose this combined information because management is using this combined information to understand how the acquisition is performing.

(c) *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 IASB should not require a company to disclose any metrics in such cases.*

According to the DP, if a company's management does not monitor an acquisition against its original expectations, the IASB concluded that requiring the company to disclose a specified set of metrics would not always produce useful information. In such a case, the IASB expected that investors would want to know that management is not monitoring an acquisition and reasons why it does not do so.

(d) *A company should be required to disclose the information about whether it is meeting those objectives for as long as its management (CODM) continues to monitor the acquisition to see whether it is meeting its objectives.*

(e) *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.*

According to the DP the IASB's preliminary view is that, if management (CODM) continues to monitor whether the objectives of the acquisition are being met, a company should be required to provide information about the acquisition's subsequent performance for as long as the information remains necessary for investors to assess whether the original objectives of an acquisition are being met. However, if management stops monitoring the acquisition before the end of the second full year after the year of acquisition, the IASB suggests that a company should be required to disclose that fact and the reasons why it did not monitor the acquisition.

(f) *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.*

According to the DP the metrics that management uses to monitor the progress of an acquisition may change over time—for example, when a company is reorganised. The IASB considers it unreasonable to require a company to continue disclosing metrics that no longer provide useful information to management and may no longer be available internally. However, changing the metrics without disclosing the reasons for that change could allow poor performance to be masked. To balance these concerns, the IASB's preliminary view is that it should not require a company to continue disclosing a metric it no longer uses internally. Instead, when a company makes such a change, it should be required to disclose that it made the change together with the reasons for the change and then disclose the revised metrics.

94 Some stakeholders, mainly preparers, have expressed concerns that detailed disclosure of a company's post-acquisition intentions together with precise targets could be commercially sensitive. According to the DP this is not a sufficient reason to prevent disclosure of information that investors need. However, some investors suggest that the information they need to understand management's objectives and to hold management accountable against those objectives may not need to be as detailed and precise as other stakeholders initially thought.

95 Some stakeholders have expressed concerns that information about management's objectives for an acquisition along with detailed targets could, in some jurisdictions, be considered to be forward-looking information that could risk litigation and should be provided outside the financial statements—for example, in management commentary—to reduce the risk of litigation. According to the DP, in the IASB's view, information about the strategic rationale, objectives and related targets for an acquisition is not forward-looking information. The information reflects management's target at the time of the acquisition. It is not a forecast of the expected outcome at the time the company prepares its financial statements.

EFRAG's tentative position

EFRAG considers that the proposed disclosure requirements could result in useful information to assess business acquisitions. However, for the requirements to be most useful, the information to be provided should not only be based on what information the CODM monitors. While EFRAG considers the information could be useful, it has some practical concerns including what information will be provided. EFRAG has not yet formed a view and is consulting its constituents on whether it is practical and appropriate to disclose the proposed information in the financial statements instead of providing the information as part of the management commentary as the information is based on management expectations and refers to non-GAAP indicators. EFRAG supports conducting additional activities to understand the issue related to commercial sensitivity. EFRAG notes that the proposed disclosures will not resolve the issues related to current goodwill accounting.

Summary of constituents' comments

96 There was mainly support to provide the information. However, some major concern was raised to the detailed requirements (commercial and internal sensitivity; verifiability and auditability; forward looking character). Field testing was recommended.

Preparers

Disclosure requirements resolve the issue identified + agreement with disclosures

97 Six participants – five preparer organisations and one preparer - opposed or had concerns with the proposed disclosures or asked to review the usefulness of the current disclosures first. One participant – preparer - agreed to disclose information about the primary reasons and business rationale for an acquisition.

98 One participant – preparer organisation - did not share how this issue is addressed in the DP. They note that in the banking sector information of key indicators and metrics on solvency, profitability, liquidity, but also on the business itself (market share, mix of products, digital capacities, etc.) are provided periodically in the form of regulatory reports, events (e.g., webcast with analyst) and through the bank's own publications. Also given that unexpected things occur, the new disclosure requirements will not be sufficient to confirm whether the price of an acquisition was reasonable and whether an acquisition has been successful. Finally, it is not easy for companies to isolate and measure the initial objectives without taking into account operational issues - IT systems integration.

99 The participant opposed to the IASB's proposal to add new disclosure requirements and particularly disagree to place this in the notes of the financial statements.

100 One participant – preparer - disagreed that the disclosures should be required in the financial statements for the reasons explained below.

(a) Purpose of financial statements: information such as showing the subsequent performance of certain investments against management's internal metrics should not be provided in the financial statements.

(b) Commercial sensitivity: An entity may make an acquisition for a strategic reason and the sole disclosure to competitors of its objectives and performance metrics could threaten the success of transaction and have detrimental impact on the entity. If required, such disclosures would put companies applying IFRS at a disadvantage to those applying US GAAP.

(c) FASBs Invitation to Comment: Requiring these disclosures in IFRS financial statements when there are no equivalent requirements under US GAAP could create an uneven playing field.

(d) How costly, verifiable and auditable: Management may be able to select a high-level strategic rationale, objectives and metrics that they want to publicly disclose and it is difficult to see how the auditors will be able to verify that. The proposed disclosure is about information that is already monitored internally so it is not supposed to be costly to obtain. In practice there will likely be costs incurred in discussions with auditors over which is the right information to disclose and how to verify and control this information.

101 One participant – preparer - was concerned that the provision of information about the performance of an acquired business might not be possible and, in any case, may lack informative value. They clarified that the purchased businesses have always been integrated in the existing ones, both in terms of management and in terms of performance evaluation.

102 One participant – preparer organisation did not share the idea of any straightforward relation between the achievement / non-achievement of the acquisition's objective and the need to impair the corresponding goodwill. By consequence, they considered that providing detailed disclosures on the achievement of these objectives (and especially any quantitative measurement of it) is useless, as far as this information does not support the measurement of financial statements' items. Such disclosures would go beyond the role of the financial statements.

103 One participant– preparer organisation - was concerned about the verifiability of the information as well as the auditability of the information. Further introducing the proposed disclosure requirements in the core financial statements would create an uneven playing field with US GAAP and might lead to information arbitrage. The participant believes that it would be much more appropriate for the information to be presented in the management commentary section of the annual report and not in the primary financial statements. Finally, they noted that some acquisitions are integrated into a wider business very quickly which makes the process of setting performance metrics and measuring the success of the acquisition impractical.

104 One participant– preparer organisation - stated the IASB proposals go too far. Instead, the statement of the disclosure objectives, accompanied by non-mandatory guidance or examples of suitable disclosure would be sufficient. Moreover, the information required by the IASB belongs to the management commentary and go beyond the realm of accounting.

105 Also, the information is based upon the expectation of management and is more subjective than the segment information. The participant wondered whether auditors will be able to validate this information. In accordance to the participant it makes senses to provide information as at the date of the acquisition about the objectives of the operation and the source of the goodwill, but this is frequently provided outside the financial statements and could be referred to in the financial statements. In their view it is not the role of the financial statements to provide quantitative information about the expected performance of the investments and this requirement would often lead to the risk of disclosure of highly sensitive nature.

106 One participant – preparer organisation - agreed with some more disclosure requirements if the case can be made that they are currently really missing and indispensable for proper understanding of the financial statements by their users. Also, the cost-benefit relationship must be evaluated. The participant notes that the better the integration process progresses, the more difficult it gets to isolate the incremental effects of the M&A transaction for the disclosure purpose only. Therefore, they ask to reconsider the disclosure requirements from a cost-benefit point of view.

107 The participant does not favour additional disclosures being required but rather recommends a comprehensive thorough review of all existing disclosure

requirements to verify if they are all still necessary, effective and whether really used by users of financial statements.

Strategic rationale and management's (the chief operating decision maker's (CODM's)) objectives

108 One participant – preparer - supported the disclosure about the primary reasons and management' strategic rationale for the business combination at the acquisition date. But they were concerned that the provision of information about the performance of an acquired business might not be possible and may lack informative value. They add that the purchased businesses have always been integrated in the existing ones, both in terms of management and in terms of performance evaluation. This would occur unless the purchased business constitutes a specific CGU. Useful information about the subsequent performance of the business combination is provided in the segment reporting and through the impairment of goodwill.

109 The participant noted it is not clear for how long the disclosure relating to the subsequent results of an acquisition should be provided. Finally, the participant considers that it should not be reported in the financial statements, but only in the management report.

110 One participant – preparer organisation - noted the management report might be the appropriate location for the additional information proposed in the DP. It seems reasonable to disclose the strategic rationale for the acquisition and the management's objectives. It may also be reasonable to require management to describe how it will monitor and assess the success of the acquisition. However, to go further than this would be damaging to entities which report under IFRS.

Not monitoring the acquisition

111 One preparers organisation noted that the requirement (iii) to state why the entity does not monitor an acquisition seems to us to be an attempt to force entities to disclose the metrics it uses by the method of "naming and shaming". In the view of the participant an entity should be allowed to state that it is monitoring the acquisition but that for reasons of confidentiality and commercial sensitivity it chooses not to disclose the metrics.

Based upon CODM reviews

112 Three participants – two preparer organisations and one preparer - noted that if the disclosures would be required, they should be based on the information and the acquisitions a company's CODM reviews. One participant- preparer - asked the IASB to perform further field tests to obtain further evidence on whether these proposals would work in practice. One participant – preparer organisation - noted this information should remain rather qualitative and materiality criteria should be considered.

113 One participant – preparer organisation - noted that setting this scope by the reference to the CODM alone might be too restrictive in some instances. If the acquisition is material it should be subject to the same communication objectives, whatever the level of internal monitoring.

114 One participant – preparer organisation - noted support for the management approach when setting up the disclosure requirements.

Commercial sensitivity

115 Seven participants – six preparer organisations and one preparer - had concerns with relation to commercial sensitivity of the information. One participant– preparer organisation was concerned that detailed disclosure of a company's post-acquisition intentions together with precise targets could be commercially sensitive and result in a disproportionate volume of disclosures with questionable quality. They were

also concerned that information about management's objectives for an acquisition along with detailed targets could, in some jurisdictions, be overly costly, difficult to audit and be considered as forward-looking information that could risk litigation. Therefore, it should be provided outside of financial statements – e.g., in the management commentary — to reduce the risk of litigation.

116 One participant – preparer organisation - was favourable to the provision of more detailed qualitative information about expected synergies, but we are opposed to any requirement to provide any quantified estimates in this respect.

117 One participant – preparer organisation - noted the commercial sensitivity is to be included in line with the similar clause in IAS 37.92 and against the tentative IASB view that it "is not a sufficient reason to prevent disclosure of information that investors need".

118 One participant – preparer organisation - noted that the requirement to provide explicitly and in detail the actual quantitative metrics used by the entity creates the risk of the entity eroding the competitive advantage the acquisition was intended to provide, by opening up the entity to the scrutiny of competitors and others who wish to benefit from such insight.

Forward-looking nature of the information

119 One participant – preparer organisation - noted information established or generated at the time of the acquisition is forward-looking by nature, even though it was determined in the past. The quantified expected outcomes from an acquisition are necessarily projections into the future of what management expects from the transaction in terms of profitability, etc. Consequently, the IASB must accept that this information is a projection into the future.

Users

120 Two user organisations supported the proposal included in the DP aiming at improving disclosures to facilitate investors to assess management's rationale for an acquisition and further consolidation. For investors it is fundamental that companies provide useful information to (1) accurately analyse the value of the acquisition, (2) the resulting value of the entity and (3) to understand the amount of the recognised goodwill. Some of their members question the usefulness and relevance of providing additional information if this information is not satisfactory. These views are based on their experience related to the level of information provided by CODMs in IFRS 8.

121 One of those participants only provided a high-level response to Question 2. They broadly agreed that there should be much better disclosure of how material acquisitions have performed against expectations and that such reporting should come from the Chief Operating Decision Maker (CODM). They liked the "disclose or explain" principle. They noted that not all acquisitions are expected to produce synergies.

122 They added that commercial sensitivity is seldom a valid excuse for non-compliance. High-level business objectives are almost never commercially sensitive, unless they relate to secret and therefore unexecuted plans.

123 Some of the participant members noted that they do not agree with disclosing information about whether an entity is meeting the objectives as they believe that the two-year period for monitoring achievement of the objectives of an acquisition is too short. In many cases, acquisitions are expected to enhance corporate value over long-term horizons of five years, 10 years, or even longer. Accordingly, some of the participant members believe disclosure should be required for as long as management continues to monitor the acquisition. Some participant members also argue that it is also necessary to consider the treatment of cases where companies implement numerous small-scale acquisitions over a single or multiple year, that are

material when taken together. Beside that high level response to Question 2 they provided upfront in their letter a list of topics Investors are interested in:

124 Price. The real acquisition price on an enterprise value basis, including non-cash transfers such as new shares in the acquirer issued to the vendor and assets injected by the acquirer into the new entity if the vendor retains a stake. In other words, the real economic value of what has been acquired and what the overall net cost has been. The cost should include acquired debts and liabilities (including quasi-debt such as underfunded pensions) and not just acquired cash. If management cannot derive the economic cost of the deal, then they should explain why this is not possible. A lot of this information can be calculated from the notes, but it can be challenging to locate, and important pieces are often missing. The full economic cost should be visible in a single place. A date of first consolidation would be useful too. Asking companies to disclose what they bought, the true economic cost and when it was first consolidated does not strike us as unreasonable. Some of these items are already required but, in their experience, compliance is patchy at best. A narrative explaining the acquisition process would also be very informative. For example, who approached whom, whether it was a competitive auction, when the process started and so on.

125 What is being bought. Adequate pro forma information on what is being acquired, including pro forma annualised revenues, operating profit and any other subtotals already published in its existing financial statements and pro forma capital expenditure (if material). This should be as contemporary as possible so investors can compare current operating performance with the economic acquisition cost. Such information would reduce uncertainty for analysts and investors. As with point above, they would expect a competent management team to have all this information readily available. They would prefer a principles-based definition of pro forma operating performance rather than a precise definition that might prove too narrow. As with acquisition price, management should be required to provide this information or explain why it is not possible.

126 Expected synergies and the timescale and cost to achieve them, ideally split between ‘hard’ (e.g., reduced overhead costs) and ‘aspirational’ (e.g., revenue synergies). Disclosure on this varies widely and some consistency and external oversight would be very welcome. As with pro forma trading, we would prefer a principles-based approach with a “provide or explain” requirement.

127 Information on whether the synergies have been achieved, while recognising that full integration may hinder measurement. Post-acquisition operating profit performance should not include the depreciation or amortisation of assets artificially created during the consolidation process as these charges are not economically meaningful. They are in effect all just disguised goodwill amortisation.

128 Adequate information to assess stewardship. One of the best ways to look at a company’s track record is to follow the operating profit or cash return on invested capital. Current accounting disclosure frequently makes this impossible or at least very difficult. For example, if the goodwill is subsequently impaired, the notes should always include the total cumulative impairment so investors can derive a meaningful value for invested capital. Quasi-goodwill intangibles should also include all historical amortisation or impairment so that investors can derive the important invested capital number.

129 Better stub period disclosure. Finally, they note that most acquired companies have a stub period, i.e., after the last audited balance sheet but before the date of first consolidation by the new owner. This period is usually not visible and investors should be informed if any unusual accounting events have occurred in this period, such as asset impairments, changed creditor terms, debt drawdown, altered

contract provisions etc. In their experience, stub periods are sometimes used for creative accounting.

130 One European user organisation detailed comments on disclosures are as follows:

Rationale – Objectives

131 Investors have to be informed about what the strategic rationale for the acquisition is and if it is in line with the overall business strategy of the entity. Also, the appropriateness of the acquisition at that particular time is relevant. This information would facilitate a better understanding and monitoring of the performance of the acquisition.

Metrics

132 They agree with EFRAG that specific information will provide a better base for understanding and valuing the entity. Hence, companies should provide metrics that are relevant for investors such as estimates of consolidated revenues, operating profits, cost savings, net earnings and balance sheet items such as consolidated debt and ROCE. Other type of non-financial information such as (combined) market share and/or other information (e.g., number of retail stores if that is the case) would also be helpful.

Price

133 When the price paid for an acquisition is larger than the fair value of the net assets acquired, a company is to recognise goodwill. Management should monitor the acquisition and has to support why the price paid is larger than the "net" fair value(s). The future performance of the acquired entity is part of the accountability of the management for the acquisition.

Monitoring

134 They agree with EFRAG's comments in paragraphs 27- 40 regarding the subsequent monitoring of the performance of an acquisition and particularly with paragraph 31. They dissent with the DP's argument that an entity cannot provide information because the acquired business is integrated. Although in certain cases the size of an acquisition at the beginning might partly condition a company to present an adequate level of information, it does not imply that the information is not required. Investors need information related to synergies in terms of costs and in terms of revenues and contribution to the total value of the combined entity.

Timing

135 They think that the information to be provided by a company after an acquisition should be in line with the time needed to complete the acquisition. Although our experience indicates that a company might take between 2 years and 3 years to fully integrate an acquisition, this will also depend on the pace of the integration and the size of the acquisition.

Sensitive Information

136 They understand that companies cannot provide commercially sensitive information but note that companies under the caption of "sensitiveness" in many cases do not provide information that in fact is not that sensitive. We agree with EFRAG's comments on paragraph 51 that a balance should be reached. Also, we support the IASB conducting additional research to understand and provide guidance related to sensitive information.

137 Regarding the forward-looking approach to disclose information that could risk litigation, they think that information related to the evolution and execution of the acquisition should not compromise the transparency of the information. They support the Board's suggestion that companies provide information in a way that

does not constitute forward-looking information, as noted in paragraph 2.31 of the DP.

Comparability

138 They observed that entities present significantly different valuations when comparing acquisitions of similar assets. This implies a great deal of subjectiveness in the valuation of the assets. Room for this subjectiveness should be reduced.

Management Commentary

139 Currently, information about the business strategy is included in the management commentary. It is important that management clearly presents the specific objective of an acquisition including information such as expected contribution to revenues and to the results of the company. Moreover, reliability and auditability of the information in M&As should not depend on the circumstances. As the process of consolidation develops new or different information might appear but the information disclosed should be reliable. Investors need material information to gauge the evolution of the acquisition and understand the merit of the price of an acquisition.

Auditors

140 One participant agreed the disclosure requirements would help investors understand the subsequent performance of the acquisition and assess whether management's objectives for the acquisition are being met.

141 They noted that disclosures about management's strategic rationale for undertaking the acquisition, the objectives of the acquisition and metrics used to monitor the acquisition may be commercially sensitive. For example, as part of the 'synergies' element of the price, a company may have planned restructurings to fully benefit from such synergies. Therefore, we suggest the IASB to consider the right balance between the benefits to investors and the commercially sensitivity of these disclosures.

142 They think that the CODM level might not be appropriate for monitoring the acquisition. The CODM typically monitors only a few very large acquisitions, important for strategic decisions. Whereas a lower management level may monitor smaller, yet material acquisitions. They suggest aligning the management level at which monitoring is done for the purpose of the disclosures to the management level involved in impairment testing as per IAS 36 Impairment of assets (IAS 36). So, they suggest the IASB considers a lower management level as the threshold for monitoring the acquisitions (e.g., the level at which goodwill is being monitored internally) and to disclose metrics used by this level of management.

143 However, they suggest the IASB to consider the relationship between these metrics and the indicators and evidence considered for impairment testing as per paragraphs 12 – 16 of IAS 36. This would become easier if monitoring is also done at a lower management level (i.e., the same as monitoring for impairment), as provided in paragraphs 7 – 10 of our response.

144 The participant agreed that in time the acquiree is fully integrated with the rest of the business, thus prompting management to stop monitoring after a certain period. Even though they support disclosing the reasons for not monitoring an acquisition anymore, they suggest the IASB to undertake a study in order to determine whether stopping monitoring 2 years after the acquisition is representative of current practice.

145 They support the IASB's requirement to disclose the new metrics and the reasons for the change if management changes the metrics it uses to monitor whether the objectives of the acquisition are being met.

146 They suggest the IASB permits these disclosures to be provided either in the notes to the financial statements or, in case this information is already presented

elsewhere and is available to users on the same terms and time as the financial statements, by cross reference to some other statement such as the management commentary. We note that some of this information may be best placed in the management commentary due to its forward looking and a non-financial nature.

147 In the participants' view, the IASB should also consider the impact of audit for these proposals. They suggest the Board field tests these proposals with users and preparers as they consist of new disclosure requirements.

Standard setters

Disclosure requirements resolve the issue

148 Nearly all standard setters supported to provide the information, with addressing some major concern at the same time.

149 One participant had doubts to the usefulness of the information requested. They noted it should be explored if that information would be better allocated as part of the management report instead of the financial statements. They noted that acquired business is often integrated with existing business and because they could be regarded as forecasts.

150 One participant noted the disclosure requirements would help investors understand the subsequent performance of the acquisition and assess whether management's objectives for the acquisition are being met.

151 One participant notes the feedback on the Post Implementation of IFRS 3 Business Combinations has clearly shown that users are asking for additional information about the subsequent performance of acquisitions. The participant understands that such information would help users more effectively assess (i) an entity's performance and (ii) management's stewardship of the entity's economic resources. Thus, the participant agrees in principle with the IASB proposals to develop additional disclosure requirements about the subsequent performance of an acquisition—i.e., disclosures about how the acquirer monitors the acquiree's performance.

152 Also, the participant had strong reservations about the following IASB proposals:

(a) the commercial sensitivity of the information entities would have to disclose applying the proposed requirements;

(b) entities' ability to provide the required information; and

(c) the location of that information—i.e., either in the notes to the financial statements or elsewhere (such as in management commentary).

153 In addition, the participant is (i) still unclear about the information the IASB expects entities to disclose in practice and (ii) unsure of whether the information that an entity's CODM currently monitors would meet the IASB expectations.

154 In the light of the challenges described above and the uncertainty about how the Board's proposals would translate in practice, the participant encourages the IASB to perform extensive field testing, reach out to stakeholders and then refine, or significantly reconsider, its proposals to strike a proper balance between the information users need and the information preparers can reasonably provide.

155 One participant agreed that the disclosure requirements will give better information about acquisitions, focusing on management strategies and the rationale for the acquisition.

156 Two participants agreed with the EFRAG answer.

157 Two participants considered the objective of the proposals to be understandable and welcomed. However, considered the gathering of the necessary information for the proposed disclosures to be difficult. This is particularly true where the acquired

company is fully integrated of an integration of the acquired company into the business of the acquirer is done. For this reason, they believe that the disclosures on subsequent performance should focus more strongly on the combined business; they suggest substantiating, amending and clarifying the disclosure objective.

158 They add that while the verifiability and auditability of the proposed disclosures may also prove difficult (e.g., with regards to possible revenue synergies), they acknowledge that other discretionary values and disclosures have to be determined and audited as well.

159 Additionally, one of the two mentions many of the relevant issues may arise in a similar way when executing and verifying an impairment test. Therefore, this argument would not be decisive for them.

160 Furthermore, they point out that the intended disclosures primarily relate to the performance of the actual acquisition transaction. When assessing the success of an acquisition, however, other – e.g., originally strategic - objectives can also play a decisive role but may be difficult to quantify in subsequent years. In addition, a comparison of what the performance would have been without the acquisition would be necessary. While these factors may limit the usefulness of the proposed disclosures, we nevertheless think that the proposed disclosures could provide additional value to investors and other stakeholders.

161 The other one of the two consider that including this type of information in the notes to the financial statement could give rise to risks for both prepares and auditors because the information could be commercially sensitive, forward looking and difficult to verify. Therefore, we think that probably the better place to collocate this kind of information is in the management commentary. They note that the FASB in its ITC issued in 2019 excludes the possibility to require information on the key performance targets supporting an acquisition and information about performance against those targets for several years after the acquisition because of concerns about: cost, complexity of integration and the forward-looking information nature of this information.

Strategic rationale and management's (the chief operating decision maker's (CODM's)) objectives

162 Four participants generally agreed with the requirements to disclose providing the strategic rationale for undertaking an acquisition and management's objectives for the acquisition. In their view they should be given on a qualitative basis in the notes. They disagree to provide information on the subsequent performance of an acquisition on a quantitative basis as becomes less relevant as time passes. These metrics are difficult to audit since they can be very subjective and should be placed in management commentary and not in the notes. They add that it may be difficult to monitor whether the objectives of an individual acquisition have been met, as the acquired business may already have been integrated in the reporting group or split amongst different business units and therefore may have become indistinguishable from the rest of the acquiring company's business.

163 One of them noted that entities should only be required to disclose information that is material. With regard to the objectives, this participant noted that requested information should be limited to indicators that the CODM monitors pursuant to the objectives set at the acquisition date. In addition, these indicators must be published as long as the CODM effectively uses them in assessing whether the acquisition is meeting its objectives—this is an essential prerequisite to the implementation of the proposed disclosures requirements. The Board should not require entities to prepare and disclose any additional metrics if the CODM stops monitoring the indicators that were defined at the acquisition date.

(Not) monitoring the acquisition – stop monitoring – change metrics

164 One participant agreed with the proposal in (b)(ii) that how management (CODM) monitors and measures the acquisition is an appropriate level of details. The metrics disclosed will give investors relevant information about how management monitors and follow up an acquisition and about how well a company is managed. With regards to quantitative disclosure requirement on such metrics the Board should emphasise that only metrics that can be measured (and audited) with sufficient reliability should be within the scope for quantitative disclosures. This would limit the disclosures with regards to metrics related to e.g., future cost savings or improvements for which limited reliable audit evidence is available.

165 The participant also supported proposal b(iii) as they see value in that investors are informed about whether an acquisition is followed up directly by the CODM or by a lower level of management either as a stand-alone entity or through integration with existing business.

166 The participant finally supported the proposal in (b)(v). Since the acquired business will change over time and often will be integrated in the total business, we find the two-year period appropriate.

167 One participant agreed that disclosing the information that the CODM does not monitor a specific acquisition might be of interest to users. Accordingly, the participant agreed with the IASB proposal that an entity should be required to disclose the fact that the CODM does not monitor an acquisition and explain why it does not do so. The participant further suggested permitting preparers to stop disclosing information about an acquisition at the earliest of (i) the end of the period during which the objectives initially set for the acquisition are met or (ii) the period during which the CODM stops monitoring whether those objectives are being met.

168 The participant agreed in principle to disclose the reasons for a change in the metrics used and the requirement to disclose the new metrics in place. However, to avoid unintended consequences, the participant recommends the IASB be cautious when developing this requirement. Because there is a risk that management might change its practices or waive monitoring new indicators to avoid disclosing a change in the metrics reviewed.

169 One participant agreed with the requirement to disclose the proposed information for as long as its management continues to monitor the acquisition in order to see whether it is meeting its objectives. They also support the disclosures required in the event of subsequent changes to the metrics used for monitoring purposes.

Based upon CODM reviews

170 Two participants suggested to consider a lower management level – at least in some cases - as the threshold for monitoring the acquisitions (e.g., the level at which goodwill is being monitored internally) and disclose metrics used by this lower management.

171 One participant emphasized that such disclosures should be built on management's metrics provided to the CODM for relevance and cost/benefit trade-off reasons. This implies that any disclosure requirements should not result in an entity providing information that the CODM does not use when monitoring the acquiree's performance. This information shall also be subject to the materiality constraint.

172 One participant supported the CODM approach for pragmatic reasons and due to the lack of a superior, sufficiently objectifiable alternative, even though not every significant transaction is likely to be reported at the CODM level.

173 One participant supported the CODM approach as that is how management (CODM) monitors and measures the acquisition. It is at an appropriate level of details. The metrics disclosed will give investors relevant information about how

management monitors and follow up an acquisition and about how well a company is managed.

Commercial sensitivity

174 Seven participants noted that the information required could trigger commercial sensitivity when disclosed.

175 One of them saw the risk of some disclosure requirements being answered met rather vaguely. Additional specific disclosure requirements should therefore not be developed, instead they would favour substantiating overarching, principle-based disclosure objectives instead. However, the specific disclosures already proposed by the IASB should be retained, as they could improve the information on the subsequent performance of an acquisition.

176 One participant thought the information can be disclosed generally without affecting the commercial situation. Exchange with preparers in their jurisdiction showed it is often possible to give relevant information to the market without harming the company. But it depends on the level of details and timing. Information about how the company will achieve the synergies, information about price expectations, specification of cost reductions and information affecting employees will often be sensitive after an acquisition.

Forward-looking nature of the information

177 One participant noted the information to be forward-looking in nature. One saw a risk that it is forward looking in nature.

178 One participant pointed out that a valid statement of objectives may also require a plausible presentation of the expected way of achieving these objectives. Therefore, they deemed a legal assessment difficult, whether information about management´s objectives for an acquisition along together with detailed targets could be considered as forward-looking information. In order to find a universally applicable suitable solution, the IASB might consider whether information classified as forward-looking in a particular jurisdiction should not be subject to mandatory disclosure for companies in that jurisdiction.

Regulators

179 One participant agreed with enhancing the information provided to investors about the subsequent performance of an acquisition and supports the disclosure of information about the strategic rationale and management's objectives for the acquisition, and about whether those are being met. They think that this information could be largely based on the information monitored by the Chief Operating Decision Maker (CODM), but that some core metrics should be defined by the Board and disclosed even if not monitored by the CODM.

180 In the participant’s view at least some key disclosures should be required for all the acquisitions which generate a material amount of goodwill, regardless of whether they are monitored by the CODM. These disclosures should include, ad minima, information about the estimated payback period, the expected profit arising from the integration of the new business(es) and the expected integration costs.

181 In addition, the participant thinks that a company should stop providing disclosures about whether it is meeting its objectives only when the synergies expected to derive from the acquisition have been realised or when those objectives have been abandoned (which in their view corresponds to the time when an acquired business is fully integrated into the acquiring business).

182 The participant agreed with the IASB's view that, in line with the existing approach in IAS 36 Impairment of Assets, information on management's objectives for the acquisition and the relevant metrics do not constitute forward looking information but rather reflect management's targets at the time of the acquisition.

183 The participant the information should be disclosed in the financial statements instead of providing the information as part of the management commentary, as this will ensure that such information is audited and enforceable. In addition, the participant thinks that generally commercial sensitivity is not a valid reason for not informing investors.

184 The participant believes that the IASB should further explore whether failure to meet the reported objectives should be linked to, and have an effect on, the impairment testing. In the context of a reintroduction of an amortisation model failure to meet the reported objectives could be considered as an indicator of impairment, thus triggering an impairment test. Such linkage would increase the usefulness of the disclosures significantly.

185 The participant suggests that the IASB takes this opportunity to further align disclosure requirements between IFRSs and US GAAP with regards to business combinations and goodwill.

Questions for EFRAG's constituents

186 As stated above, EFRAG considers that the disclosures proposed in the DP could provide useful information. EFRAG has, however, not yet formed a view on whether the financial statements are the right place to disclose information about the performance of an acquired business compared with management expectations. Among other things, it might be difficult to audit the information if Standards do not provide guidance on how the non-GAAP metrics should be determined.

(a) *Do you agree with the IASB's proposal to include the proposed information in the notes to the financial statements? Why/why not? If you disagree with the IASB, do you think it could be included in the management commentary?*

(b) *Do you think that the specific information would be more useful, relevant and/or reliable, if it is audited?*

(c) *Do you think it would be possible to audit the information/prepare the information in a manner that would make it possible to audit it?*

(d) *Paragraph 42 above states that EFRAG expects that the requirement to disclose that an entity is not monitoring an acquisition could create a market discipline. If you are a user of financial statements, how would it affect your analysis if you receive information that an entity is not monitoring a significant acquisition?*

(e) *The IASB considers that it is possible to disclose useful information on the level of achievement of the financial or non-financial targets initially defined at acquisition date and of expected synergies (see Question 4 below), without triggering commercial sensitivity. EFRAG is interested in understanding whether constituents agree with this approach and would like to receive practical examples in this regard.*

(f) *Would there be any constraints within your jurisdiction that could affect an entity's ability to disclose the information proposed in the DP? If so, what are those constraints and what effect could they have?*

Preparers

Notes to the financial statements vs management commentary

187 Six participants – five preparer organisation and one preparer- were not in favour of including this information in the notes of the financial statements from a cost/benefit perspective as they do not share the view that it would be more useful, relevant or reliable if audited. One of them – preparer organisation - noted that putting the information in the management commentary would not make such a big difference.

188 They note that audit would create unnecessary costs, would add complexity and the benefits would be limited. Including this information in the management commentary would not be make such a great difference. They also concur with the idea that providing this information outside the financial statements would reduce the risk of litigation.

189 Five participants – three preparer organisation and two preparers - noted the information should be provided in the management commentary. One of them added similar information is already provided to investors outside of the financial statements. In their view, they did not think it would be relevant to make it subject to audit. It is not obvious either, whether and how the auditors would be able to verify this management information.

190 One participant – preparer organisation - supported the IASB's overall objective of improving acquisition-related information provided to stakeholders. However, we consider that this information should be limited to the acquisition's objectives determined prior to the acquisition, in order to avoid a disproportionate volume of disclosures of limited usefulness and unjustified cost.

191 They were also concerned that information about management's objectives for an acquisition, along with detailed targets could, in some jurisdictions, be overly costly, difficult to audit and considered to be forward-looking information that could risk litigation. It should therefore be provided outside of financial statements: for example, in a management commentary, to reduce the risk of litigation.

192 Furthermore, an acquisition is generally a long-term project and the overall objective may only be achieved over a long (e.g., 10- or 15-years) period, whereas any interim assessment may show discouraging results.

More useful if audited / possible to audit

193 One participant – preparer organisation - noted that in the insurance industry, many acquisitions are based on cost synergies, because it is expected that managing larger portfolios of contracts will provide cost savings. However, tracking these cost savings along the subsequent periods after the acquisitions for the purpose of a disclosure may be difficult, unreliable and thus irrelevant for the users.

Commercial sensitivity

194 Seven participants – six preparer organisation and one preparer - had concerns with relation to commercial sensitivity of the information. One participant – preparer organisation - was concerned that detailed disclosure of a company's post-acquisition intentions together with precise targets could be commercially sensitive and result in a disproportionate volume of disclosures with questionable quality. They were also concerned that information about management's objectives for an acquisition along with detailed targets could, in some jurisdictions, be overly costly, difficult to audit and be considered as forward-looking information that could risk litigation. Therefore, it should be provided outside of financial statements – e.g., in the management commentary — to reduce the risk of litigation.

195 One participant – preparer organisation - was favourable to the provision of more detailed qualitative information about expected synergies, but we are opposed to any requirement to provide any quantified estimates in this respect.

196 One participant – preparer organisation - noted the commercial sensitivity is to be included in line with the similar clause in IAS 37.92 and against the tentative IASB view that it "is not a sufficient reason to prevent disclosure of information that investors need".

197 One participant – preparer organisation - noted that the requirement to provide explicitly and in detail the actual quantitative metrics used by the entity creates the risk of the entity eroding the competitive advantage the acquisition was intended to

provide, by opening up the entity to the scrutiny of competitors and others who wish to benefit from such insight.

Auditors

198 One participant – preparer organisation - generally referred to its answers provided to question 2. The participant was not aware of constraints that could affect an entity's ability to disclose the information proposed in the DP.

Standard setters

Notes to the financial statements vs management commentary

199 Eighth participants noted disclosures about the performance of an acquisition could be more appropriate to include it in the management commentary. One of them noted that if amortisation of goodwill is reintroduced the disclosures are not necessary.

200 One of them recommended the IASB to reach out to preparers in various jurisdictions and industries to better understand the existing practices and the difficulties that disclosing the CODM's indicators could entail. Should there be ground to distinguish between indicators – some being within the scope of the management commentary, others within the scope of the notes to the financial statements – the Board should develop application guidance to help entities identify where they should provide information.

201 One participant believed that the disclosure of forward-looking information and the expectations from an acquisition do not meet the general purpose of accounting and therefore does not support the development of proposals to add disclosure objectives to provide additional forward-looking information.

202 One participant noted the explicit objectives and subsequent performance of an acquisition would probably contain non-GAAP indicators and forward-looking information. In general, information with a forward-looking nature is included in the outlook paragraph of the management commentary. If the IASB decides to disclose such information in the financial statements, this is a fundamental change compared to the current information requirements in IFRS.

203 The participant questioned whether the information as proposed should be part of the financial statements or instead should be part of the management commentary. They recommend the IASB to further explore whether this information should be part of the financial statements or management commentary and other aspects, like the commercial sensitivity of the proposed information.

More useful if audited / possible to audit

204 Three participants noted the information provided by the companies will be more useful or relevant and/or reliable if it is audited. One of them understood that if the purpose is that the entities can provide real information that they are using in their decision-making process, to prepare the information in such a way that it is verifiable by an auditor will be difficult, since each manager will prepare the information depending on the management procedures that the company follows.

205 One participant thought it would be possible to prepare the information in a manner that would make it possible to audit.

206 Seven participants noted the information is difficult to audit or creates auditability issues. One of them thought that the verifiability of the information supporting the proposed disclosures is a real practical issue. Many of the metrics the CODM uses may be non-financial (such as market shares) and, if having a financial nature, may not be defined by IFRS Standards. In addition, part of the information an entity would disclose would reflect management's expectation and thus, be forward-looking in nature.

207 One of them noted while the verifiability and auditability of the proposed disclosures may also prove difficult (e.g. with regards to possible revenue synergies), they acknowledged that other discretionary values and disclosures have to be determined and audited as well. Additionally, many of the relevant issues may arise in a similar way when executing and verifying an impairment test. Therefore, this argument would not be decisive for them.

What if an entity is not monitoring an acquisition

208 One participant expected a CODM to monitor all relevant business acquisitions for the entity. In case of a disclosure that an entity is not monitoring an acquisition, we assume that any missing information is not considered relevant for the financial statements as a whole and its stakeholders.

Commercial sensitivity

209 One participant noted disclosures about the performance of an acquisition could be a sensible information.

210 One participant thought it might depend on the required level of detail whether the proposed disclosures of (objectives and subsequent performance of) an acquisition triggers commercial sensitivity. A similar approach as currently included in IAS 37.92, where an entity can (only) revoke from disclosure based on an expected serious prejudice of the position of the entity, could be considered by the IASB to potential commercial sensitivity conflicts as part of this proposal.

Existence of constraints

211 One participant noted some existing constraints. For example, the capital companies law in its article 197 Right of information in the public limited company, in section 3 states that company administrators will be obliged to provide the information requested (under the two previous sections), unless this information is unnecessary for the protection of the rights of the partner, or there are objective reasons to consider that it could be used for extra-social purposes or its publicity damages the company or related companies.

212 Three participants were not aware of any constraints which prevent an entity in their jurisdiction to disclose the information proposed in the DP.

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?

Proposals in the DP

213 In the IASB's view, investors need to understand why a company acquired a business, and what assets, synergies and other benefits it paid for. They use this information to assess whether the price for the acquired business is reasonable. Investors also want to understand whether management's objectives for an acquisition are being met.

214 Thus, the IASB's preliminary view is that it should develop a proposal to add further disclosure objectives that require companies to provide information to help investors to understand:

(a) *the benefits that a company's management expected from an acquisition when agreeing the price to acquire a business; and*

(b) *the extent to which management's (CODM's) objectives for a business combination are being met.*

EFRAG's tentative position

EFRAG supports the introduction of the disclosure objectives, should the proposed information be included in the notes to the financial statements.

Summary of constituents' comments

Preparers

215 Six participants – five preparer organisations and one preparer - agreed with the usefulness of providing this information to investors but almost all of them also raised concerns at the same time.

216 One of them – preparer organisation - noted an alternative approach should be considered in relation to highly regulated sectors, such as the banking sector. They added that at present, banks inform about the management's specific objectives for an acquisition to the market as at the acquisition date. The requirement to include that information in the notes of the financial statements would provide limited benefits and would increase costs, so we would expect more flexibility in this regard.

217 One of them – preparer - had reservations about the disclosure objective to help investors understand the extent to which an acquisition is meeting management's (CODM's) objectives for the acquisition.

218 One of them – preparer organisation - was concerned that the disclosure objectives presented in this discussion paper will lead to increased financial statement complexity and increased audit cost burden. We believe that some of the proposals are not only commercially sensitive, but also overly complex and require significant judgement.

219 One preparer organisation agreed with the objectives provided that this does not result in the systematic disclosure of quantified sensitive information and that can be done by reference to information that is communicated through other vectors (such as the management report). They made a counterproposal as follows:

(a) Establish the principles and objectives of disclosures;

(b) Then allow entities to define the information that they judge to be relevant to achieve these objectives, and to help them by suggesting information which might make sense but without making it mandatory.

220 One preparer organisation found the disclosure objectives reasonable. They suggested to provide non-mandatory examples of what could be disclosed in order to help entities to arrive at a suitable set of information which would represent a good balance between cost and usefulness without destroying entities' competitive advantages.

Users

221 One user organisation broadly agreed with the IASB proposals but noted the usefulness of such disclosure may be limited as they cannot envisage many companies stating that an acquisition will produce minimal benefits and does not meet the CODM's objectives.

Auditors

222 One participant understood that disclosures about the benefits expected from the acquisition would help investors understand the rationale behind the price.

However, such information may sometimes be commercially sensitive. They note that disclosures about the extent to which an acquisition is meeting management's objectives may result in boilerplate disclosures. They ask the IASB Board to consider this.

Standard setters

223 Four participants considered such information will be useful. One of them noted the information would be useful when included in the notes to the financial statements in order to learn about the strategic rationale and management´s objectives for an acquisition as at the acquisition date and also information on whether the entity is meeting the goals. One of them noted the disclosures would help investors understand the rationale behind the price but noted such information may be commercially sensitive. Another one considered the disclosures should focus on benefits the company's management expects from the acquisition and subsequent measurement of whether those expectations were fulfilled. The proposed disclosure objectives related to the expected benefits from the acquisition place strong stewardship on management and will strengthen corporate governance. Finally, one participant agreed with the EFRAG answer.

224 Two participants agreed in principle with broadening the existing disclosure requirements but asked first to seek feedback on disclosure objectives or to better substantiate them.

225 One of them questioned the consistency of the approach retained by the IASB. In the participants', it would have been more relevant to first seek respondents' feedback on proposed disclosures objectives and then consider developing requirements.

226 One does not support the development of proposals to add disclosure objectives to provide additional forward-looking information as they believe that the disclosure of forward-looking information and the expectations from an acquisition do not meet the general purpose of accounting.

Level at which the performance of an acquisition is monitored

227 The participant notes that many business combinations end up with a swift and deep integration of the acquiree within the acquirer's legal, organisational and operational structures. This results in entities monitoring the acquiree's subsequent performance through the performance of one or several operating segment(s). This may make particularly difficult, if not impossible, to monitor the acquiree's specific performance against the objectives set at the acquisition date. As a result, any disclosures objectives should therefore clearly set out that an acquisition's performance could be monitored at a higher level than the acquiree itself. This, in turn, should lead to disclose information about the level at which the acquisition is monitored.

The need to consider the practical challenges identified when developing disclosure objectives

228 The participant recommends the IASB make a thorough analysis of the metrics currently used by entities before developing new disclosure objectives. Furthermore, they think those disclosures objectives should acknowledge that an entity would provide information in the notes to the financial statements or in the management commentary. They suggest distinguishing between:

(a) the benefits expected from the acquisition—that information should be located in the notes to an entity's financial statements.

(b) the metrics the management intends to review to monitor such benefits and the extent to which the acquisition is meeting management's objectives—

that information should be located in the management commentary or other financial communication.

229 Another one opined that it would be more helpful to further substantiate the basic disclosure objectives. They suggested developing overarching, principle-based disclosure objectives in conjunction with (limited) disclosure requirements for core-information. They thought that the proposed disclosures on the subsequent performance of an acquisition could provide additional value to investors and other stakeholders and should therefore be part of that core- information.

230 Similarly, adding disclosure objectives to aimed at providing users with information on the benefits that a company's management expected from an acquisition when agreeing on the price to acquire a business and on the extent to which an acquisition is meeting management's (CODM's) objectives for the acquisition could help in identifying and preparing useful information.

Regulators

231 One participant agreed with the IASB preliminary view that it should develop, in addition to the proposed new disclosure requirement, proposals to add disclosure objectives to provide information to help investors to understand the benefits a company's management expects from an acquisition and the extent to which an acquisition is meeting the CODM's objectives.

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?

Proposals in the DP

232 According to the DP, investors have said the information they want is not about goodwill itself, but information that gives them a better understanding of why a company paid the price it did for the acquired business.

233 Investors have said that information on the nature, timing and amount of expected synergies is important. It would allow them to understand better the benefits a company's management expected when agreeing the price to acquire a business. This information would help investors to assess whether the price paid was reasonable. The information would also help investors hold management to account for its progress in achieving those synergies.

234 Stakeholders have told the IASB that synergies are often difficult to quantify. However, the IASB expects that management would have already made an estimate of expected synergies in agreeing the price for an acquired business. Stakeholders have also said that disclosures about expected synergies could be commercially sensitive. However, the IASB does not intend to require companies to disclose detailed plans on how they intend to realise the synergies.

235 Thus, the IASB's preliminary view is that it should require a company to disclose in the year an acquisition occurs:

(a) *a description of the synergies expected from combining the operations of the acquired business with the company's business;*

(b) *when the synergies are expected to be realised;*

(c) *the estimated amount or range of amounts of the synergies; and*

(d) *the estimated cost or range of costs to achieve those synergies.*

236 In addition, investors would like companies to disclose the amounts of financing and defined benefit pension liabilities because they view them as part of the total capital employed in the transaction by the acquirer.

237 Thus, the IASB's preliminary view is that it should develop proposals to specify that liabilities arising from financing activities and defined benefit pension liabilities are major classes of liabilities.

EFRAG's tentative position

EFRAG considers that the suggested disclosure requirements on synergies could provide useful information. Similar disclosures for other components of goodwill could equally provide useful information. However, EFRAG questions whether the information should be provided in the financial statements and whether the benefits of providing the disclosures on synergies under a quantitative perspective will outweigh the costs. EFRAG supports separate disclosure of liabilities arising from financing activities and defined benefit pension liabilities acquired as part of an acquired business.

Summary of constituents' comments

Preparers

Rationale – Objectives

238 While two respondents recognised that information on synergies underlying the proposed disclosures provides investors with useful information, many of the respondents believed that similar information is already provided to investors in the management commentary and in other communication to investors outside the financial statements. One respondent specified that, in his experience, information provided seemed to meet users' expectation.

239 One respondent considered that the IASB's views on acquisition objectives are excessively focused on synergies. Other objectives may also be relevant on a case-by-case basis (i.e., objective of penetration of new markets). Therefore, the other possible objectives of an acquisition should also be considered by the IASB.

Sensitive information

240 Many of the respondents considered the proposed disclosures on synergies to trigger commercial sensitivity issues.

241 One of them commented that, while he would not oppose to providing more detailed qualitative information about synergies, he would disagree with any requirement to provide quantitative information. In his view, it would trigger the revelation of both external (i.e., costs and competitive strategies) and internal (i.e., restructuring or other plans before an official announcement) sensitive information.

242 Two preparers' organisations expressed their concern that providing the proposed disclosure might have a negative impact on the competitive position of the reporting company, including the creation of a significant divergence from other major

accounting frameworks, such as the US GAAP, that would place IFRS-only reporters into the uneven playing field and might lead to information arbitrage.

243 One preparers' organisation expressed its concerns that highly sensitive information might be given: (i) to competitors (i.e., margins, costs and competitive strategies); (ii) to employees (in case of restructuring or other plans in advance of a proper announcement); and (iii) to clients, who might take advantage of this to demand a share of the expected synergies through a reduction in the price charged to them. It also shared that an acquisition may be a first step toward a broader commercial development strategy that will give rise to future acquisitions on which the entity does not wish to communicate yet.

244 A preparer organisation consider that no sensitive information should be provided in the financial statements beyond that which is required in the relevant jurisdiction as part of the prospectus and acquisition documentation that has to be provided to shareholders in order for them to approve the transaction. Any additional requirement would trigger a risk of potential litigation. In addition, they do not agree with the statement made in the DP that information about expected synergies is not forward-looking information. In their view, these estimates reflect management's expectations of what can be achieved and are clearly forward-looking estimates. It would be unwise to provide any such sensitive quantified detail, since such quantified estimates could be deemed to be formal commitments.

Complexity and incremental costs

245 One respondent commented that, although the information goes through an exhaustive approval process when communicated to the market (see paragraph 89), it is based on forward-looking statements, projections, objectives, estimates and forecasts which involve known and unknown risks, uncertainties and other factors, which may cause actual results, performance or achievements of a company to be materially different from those expressed or implied by these forward-looking statements. It generally cautions investors not to place undue reliance on such forward-looking statements as a prediction of actual results.

246 One respondent reported its concern about verifiability and auditability of the information to be provided (which would essentially be comprised of non-GAAP measures) as well as due to the amount of judgement and estimation that the preparation of the disclosures would require.

247 Three preparers organisations were against producing the amount of information requested by the proposed disclosures under a quantitative perspective. Two of them argued that it would imply a significant judgement and incremental costs or imply the risk of negative consequences that would outweigh benefits. One other considered that, whereas entity's management can accept the fact that the estimations it uses might turn out differently, external users might not be so accepting of the same level of uncertainty.

No clear definition of 'synergies'

248 One respondent highlighted the current lack of clear definition on how a synergy should be estimated. In his view, increasing the comparability between companies through the proposed disclosure would be complex to achieve.

Placement of information

249 All the respondents that provided specific input on this issue (four respondents) considered that, based on considerations included in paragraph 245, they would consider the management commentary the most appropriate placement for this disclosure.

Additional proposals or other considerations on synergies

250 A preparers organisation questioned the proposed disclosures to be required for all instances where an acquisition has generated significant amounts of goodwill, regardless of whether these are monitored by the CODM or not. Such a different scope compared to the other disclosures requirement (set at the CODM level) could lead to a loss of consistency in the information communicated as a whole.

Financing and pensions liabilities as major classes of liabilities

251 A preparers' organisation and one other respondent agreed with the proposals.

252 A preparers' organisation considered that it is not necessary to specify that liabilities arising from financing activities and defined benefit pension liabilities are major classes of liabilities. In its view, the requirements of current IFRS 3.B64 when read in conjunction with IAS 1 are sufficiently clear. Such disclosures are subject to materiality and management judgment.

Users

Rationale – Objectives

253 One respondent commented that the more specific the information, the better for investors. In this context, users would like to know in a quantifiable manner what are the synergies and estimated contribution to results of the combined business.

254 One respondent considered that synergies are seldom hard numbers and an excessive focus on short-term savings can cause long-term damage. It noted that is important that the IASB would not unintentionally create an environment where management will focus on hitting short-term synergy targets at the expense of longer-term stewardship, as bad drafted standards could lead to undesirable management behaviour.

Sensitive information

255 One respondent acknowledged preparers' reluctance to disclose sensitive information and recognised the need to find an appropriate balance between investor needs and preparers willingness to disclose this information. However, it commented that companies often leverage the caption of "sensitiveness" to avoid providing information that in fact is not that sensitive.

256 This respondent also supported the IASB conducting additional research to understand and provide guidance related to sensitive information.

Complexity and incremental costs

257 One respondent disagreed with the argument that an entity cannot provide information because the acquired business is integrated, as investors need information related to synergies in terms of costs and in terms of revenues and contribution to the total value of the combined entity.

Additional proposals or other considerations on synergies

258 One respondent noted that expected tax synergies, where material, should also be disclosed

Auditors

Rationale – Objectives

259 One respondent agreed that disclosures on synergies would help users to better understand the potential impact of an acquisition on the combined financial statements of an entity and would make management more accountable for its decision. However, he considered that, even if he acknowledged that investors seek information about synergies (as part of goodwill) in order to justify the price for the acquisition, expected synergies do not necessarily reconcile to or explain in full the

consideration transferred and goodwill (as they are not necessarily a subtotal of goodwill and they may be, for example. greater than the respective element in goodwill).

Sensitive information

260 One respondent recognised that the disclosure can trigger commercial sensitivity (i.e., planned restructuring to fully benefit from the synergies). However, it commented that the current proposal on synergies appears to appropriately strike a reasonable balance with preparers' concern for commercially sensitive disclosures.

Complexity and incremental costs

261 One respondent suggested, under a cost-benefit perspective, that the Board would provide an exemption for disclosing amounts and costs of synergies if such information is not readily available. Under this exception, preparers would be expected to disclose such information only if it has been gathered in the deal process.

No clear definition of 'synergies'

262 One respondent suggested that further clarifications and definitions of some terms on proposals of synergies disclosure should be considered by the IASB. In his view, in case as a standardised approach, rather than a management approach, should be followed, the requirement should be as specific as possible, including: (i) a clear definition of 'synergies'; (ii) specifying whether 'estimated amount or range of amounts of the synergies' relates to synergies in total or to each type of expected synergy; and (iii) clarifying if a detailed pattern of synergy realisation by type (or in total) or simply a timeframe by type (or in total) should be disclosed.

Additional proposals or other considerations on synergies

263 One respondent suggested that the IASB considers proposing disclosures of subsequent changes in the initial synergy expectations as these may be useful for assessing the performance of an acquisition and are interrelated with disclosures on subsequently monitoring an acquisition.

264 One respondent considered that the IASB should clarify whether the proposed disclosures on synergies should be based on management's synergy expectations in the deal process or after closing of the transaction. In his view, it can be relevant as, while synergy expectations initially included in the deal model will explain better the agreed purchase price, the synergy expectations as of closing might be a better benchmark to assess the subsequent realization of synergies, and thus performance of the acquisition.

265 One respondent raised a discrepancy between the disclosures on expected synergies being provided for all transactions with material synergies and the disclosures on management objectives and subsequent performance for an acquisition being provided at the CODM level. He suggested the IASB to better aligned these proposals.

Financing and pensions liabilities as major classes of liabilities

266 One respondent agreed with the proposals, as beneficial for investors and easily available to preparers.

Standard setters and regulators

Rationale – Objectives

267 Almost all respondents considered that the disclosures on expected synergies would provide useful information to investors to better understand the potential impact of an acquisition on the combined financial statements of an entity. Two of them commented that the benefits from them would outweigh the costs.

268 One respondent recommended that the IASB design future requirements in a way that may be clear and enforceable, leading to a disclosure specific and informative rather than a boilerplate information.

Sensitive information

269 Some respondents recognised that the disclosure can trigger commercial sensitivity. One of them argued that sensitivity issue would affect entities both toward competitors under a commercial perspective (i.e., revenues synergies) and toward other stakeholders (i.e., cost synergies). One respondent also mentioned the risk of creating a competitive imbalance between entities applying IFRS Standards and those applying other GAAPs, encouraging the IASB to consider setting out disclosure requirements in relation to acquisitions after having carefully considered the requirements in other major accounting frameworks.

270 One respondent suggested that the requirements would give some leeway to companies in relation to the information they would be required to disclose. Accordingly, based on its judgement, management would select information that is relevant to the circumstance without being prejudicial to their financial performance or competitive position.

271 Two respondents noted that, consistently to other disclosure requirements, a balance between the benefits to investors and the commercially sensitivity of these disclosures should be found.

Complexity and incremental costs

272 Many respondents commented that the quantitative determination of this figure could represent a significant cost for preparers, and would be also complicated to audit, as mostly based on management's assumptions It would be also subject to a high degree of judgement and therefore lack of verifiability. Two of them would then favour the disclosure to be provided on a qualitative basis only. One respondent suggested the IASB should consider doing more fieldwork to investigate if the proposed disclosure is in fact information that management produces today and can easily provide in the financial statements without undue costs.

273 Two respondents acknowledged that the proposed information may be difficult to verify and audit. However, as some other discretionary values and disclosures have to be determined and audited as well (including the impairment test), this argument was not decisive for them in order to conclude that the disclosures would not to be provided.

274 A respondent indicated that the disclosure of information about synergies is subject to some limitations, including the availability of that information itself. Entities do not systematically undertake business combinations to benefit from synergies. Accordingly, an entity should be required to disclose information about synergies only if that information is available. In addition, concerns have been raised about the IASB's proposals resulting in entities tracking synergies for disclosure purposes as they would incur significant implementation costs.

275 One respondent, who agreed that the Board should develop proposals that require companies to disclose expected synergies and when the synergies are expected to be realized, do not consider that the disclosure should include detailed requirements about estimated amount or range of amounts of the synergies, and the expected cost or range of costs to achieve those synergies as there should be reliability threshold, as included in other standards, before quantitative information should be disclosed. In its view, mandating such a disclosure seem to conflict with the overall direction of the DP, which is to report on metrics that are reported to the CODM. Another respondent, noted in a similar line, that quantitative information is often subject to significant estimation uncertainty. In its view, the existence of significant estimation uncertainty may warrant not publishing that information.

Placement of information

276 Based on the consideration that information to be provided are forward-looking and mainly consists of management views, a respondent considered the proposed disclosures to be better placed in the management commentary.

277 A respondent, when coming to the same conclusion, added the auditability issue as an argument.

No clear definition of 'synergies'

278 One respondent commented that an informative guide on the concept of synergies should be developed to standardize the responses provided by the entities, as well as to reveal the factors that influence in the calculation of synergies.

279 One respondent noted that as synergies are not well defined and it would be difficult to have it audited when provided under a quantitative perspective.

Additional proposals or other considerations on synergies

280 Notwithstanding what stated at paragraph 272, one respondent considered that it would be useful to report the projected data and justify the differences with the results achieved, at least for the first year or the current year in relation to what was estimated in the previous year and see if there have been relevant changes in the hypotheses considered in the initial moment.

281 One respondent suggested the IASB to explore whether the proposed disclosures should be provided for individually not material acquisitions are material when collectively considered (as it is foreseen for other types of disclosures by IFRS3 paragraph B65).

282 Regarding EFRAG's consideration about the opportunity to provide similar information for other components of goodwill, respondents argued that:

(a) This suggestion would be carefully considered under a cost-benefit perspective. Under this proposal, it considered that, other than synergies, the residual formed mainly by intellectual capital or other assets generated that do not meet the requirements for recognition as an asset could be highlighted.

(b) Businesses can be acquired by management for several reasons, such as expected synergies, increase of market share or product development/ research and development purposes therefore synergies are not always the main objective for management to acquire businesses and therefore these proposals (DP) will not always be helpful to hold management accountable for the acquisition. In its view disclosures should follow a 'management-approach'. Hence, any proposed disclosures of metrics on expected costs and benefits from an acquisition should not only be focussed on synergies but must be broadened.

(c) Restricting the scope of disclosures to synergies only may not meet users' needs regarding goodwill analysis. Additionally, considering synergies as the single most important component of goodwill might be misleading. Business combinations may indeed be undertaken for reasons other than primarily benefiting from synergies Therefore, the requirement to provide disclosures about synergies may not provide useful information for any business combination. Accordingly, the Board should not prevent entities from disclosing information about other objectives. Nevertheless, this respondent noted that the Board should not require entities to disclose an exhaustive quantitative analysis of the components of goodwill as, among various reasons, it seems impractical.

283 One respondent indicated that providing quantitative disclosures about synergies included in the balance of goodwill would raise a conceptual issue. The amount of synergies is estimated considering the acquiree as a whole at the acquisition date (including synergies attributable to non-controlling interests). However, the amount of goodwill recognised in the statement of financial position might not systematically include amounts attributable to non-controlling interests. Therefore, in its view, the estimated amount or range of amounts of the synergies that an entity would disclose could be misleading and could lead users to overestimate the relative importance of the synergies to be achieved with respect to the objectives set for the acquisition as a whole.

Financing and pensions liabilities as major classes of liabilities

284 Many of the respondents that provided a reply agreed with the proposals, as beneficial for investors and easily available to preparers.

285 A respondent disagrees with the requirements for liabilities arising from financing activities and defined pension plans. In its jurisdiction, defined benefit plans are being phased out, and liabilities are normally settled as part of the acquisition. In addition, IAS 7.44B already requires disclosure of changes in liabilities from financing activities arising from obtaining control of a business and IAS 19.141(h) requires the disclosure of the effect of business combinations as part of the reconciliation of the net defined benefit liability (asset). In this regard, it does not support duplicating those disclosure requirements.

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?
>
> (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?

Proposals in the DP

286 During and after the Post-implementation Review of IFRS 3, stakeholders commenting on pro forma information have said that:

(a) *the information is not useful because it is hypothetical;*

(b) *there is a lack of guidance on how to prepare the information and therefore companies prepare the information in different ways;*

(c) *information about the revenue and profit of the acquired business before the acquisition is not always readily available;*

(d) *it is costly to produce the pro forma information.*

287 The IASB reached a preliminary view that it should:

(a) *Replace the term 'profit or loss' in paragraph B64(q) of IFRS 3 with the term 'operating profit before deducting acquisition-related costs and integration costs'. Operating profit or loss would be defined as in the Exposure Draft General Presentation and Disclosures. The IASB expects that a measure based on operating profit would:*

(i) *provide investors with information about the operating performance of the main business activities of the acquired business that is independent of how the acquired business is financed; and*

(ii) *avoid the need for companies to make subjective allocations of finance costs and tax expenses if the acquired business has been integrated.*

(b) *Add to paragraph B64(q) a requirement to disclose cash flows from operating activities. The IASB expects that the disclosure of cash flows from operating activities would help those investors who use cash flow measures in their analysis.*

(c) *After the revisions in (a) and (b), retain the requirement for the information to be disclosed for the combined entity as if the acquisition had occurred at the start of the reporting period (pro forma information).*

EFRAG's tentative position

EFRAG suggests that the IASB provides a principles-based definition for the new concepts of 'acquisition-related' and 'integration cost' to be used in preparing the pro forma information. EFRAG agrees with replacing 'profit or loss' with '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. EFRAG disagrees with providing similar information for cash flows from operating activities.

Summary of constituents' comments

Preparers

288 One preparer agrees that the requirements in IFRS 3 should be retained. However, it suggests that it would be beneficial to allow the disclosure of revenue and profit or loss of the acquiree for the period before the acquisition date rather than the current required information.

289 Another preparer agrees with the EFRAG position but does not support the proposal to provide information related to the acquired business after the acquisition date.

290 Another respondent agreed that there are practical problems and diversity in the preparation of the proforma information which impairs the meaningfulness and comparability of the disclosure. Therefore, it disagrees with retaining this disclosure but considers the proposed post-acquisition disclosures more useful than the current IFRS 3 disclosures. It agrees with replacing 'profit or loss' with 'operating profit' as defined in the ED *General Presentation and Disclosure* but considers excluding acquisition-related and integration costs would impair comparability and reliability of the disclosure.

291 A preparer organisation agrees with proposals around operating costs but are opposed to further guidance and are concerned that IASB is attempting to standardise the presentation of the income statement in this manner. They consider that the underlying principle should be that entities with significant acquisition costs in operating result to exclude these costs. On integration costs they consider that this may be sensitive and not tracked by everyone and a principle is required to allow entities with material integration costs to eliminate these if required. They also stated that the costs related to disclosure of cash flows from operating activities would be significant and did not consider the IASB's reasoning convincing.

292 An insurance preparer organisation considers that actual rather than hypothetical information should be presented in the financial statements. This would render additional guidance unnecessary. They propose any changes to IFRS 3 until the ED *General Presentation and Disclosures* have been finalised. They would also rather call goodwill 'acquisition premium' to indicate faithfully its nature to users.

293 Another preparer organisation with retaining the current requirements, however, they emphasize that the preparation of such information can be very onerous, e.g. if the target does not apply IFRS. Therefore, significant assumptions will be required and the reliability of the numbers before the acquisition will not be comparable to those after the acquisition. The respondent does not consider that further guidance is required as sufficient experience and best practice have been developed. The respondent considers that IFRS 3 should only be adjusted after the DP on *General Presentation and Disclosures* have been finalised and pointed out that it is not clear whether these costs would qualify for exclusion under the DP proposals. The respondent is unconvinced about the merit of the proposed cash flow metric and considers that it would require significant costs to produce.

294 Another preparer organisation disagrees with the proposed cash flow disclosures due to cost and not being useful without disclosures about the basis of preparation.

Users

295 One user organisation states that the current proforma disclosures are almost universally unsatisfactory and that the standard should focus on providing companies with robust guidance rather than being overly prescriptive. The respondent considers that the proforma numbers should exclude the impact of the purchase price allocation as these do not impact cash flows or management rationale for the acquisition of a business. The respondent identifies two problems with the current disclosures:

(a) firstly, the timing of an acquisition may only be later in the financial year and exacerbate undisclosed seasonality; and

(b) secondly, the profit or loss number is not the operating metric investors would like to see.

The respondent would like to see proforma revenue and operating profit numbers for a 12-month period for all material acquisitions. The period can be left to management discretion but should be as recent as possible. The operating profit should exclude non-recurring items such as integration expenses, the impact of inventory write-ups, amortisation of quasi-goodwill intangibles and asset write-downs.

Auditors

296 One respondent is concerned that with IFRS 3 the proposals will lead to boilerplate and costly disclosures but supports more guidance to be issued by the IASB on the preparation of such information. Consistency and auditability would be improved if the IASB requires the disclosure of the basis of preparation. The respondent also agrees with the disclosure of 'operating profit before deducting acquisition-related costs and integration costs' but suggests that the IASB provides guidance on what

costs would be deducted. The respondent also agrees with the proposed disclosure of cash flows from operating activities as this would help investors in their cash flow analysis. However, with the current requirements in IFRS 3, the disclosures may be voluminous and costly, so they suggest that the IASB field tests the proposals of the exposure draft resulting from this DP in order to be efficient.

Standard setters and regulators

297 Two respondents consider that the IFRS 3 information should continue to be disclosed but considers that further guidance is required about acquisition-related and integration costs. One of these is also concerned about the cost-benefit trade-off as preparers do not currently have this data. The other considers that the disclosure of cash flows from operating activities is important as this helps investors in their cash flow analysis. Another respondent disagrees as it would include too many discretionary decisions and moreover, the usefulness of one cash flow figure is very limited.

298 One respondent agrees that the IFRS 3 requirements should be retained but consider that the IASB should consider whether the benefits exceed the costs of proforma information before expanding on these requirements. The respondent also suggests leveraging regulatory information required in this regard such as those of market regulators[2]. Developing guidance about the preparation of proforma information may be useful, including specifying the objectives of such information or the basis of preparation. The respondent has reservations about the proposed disclosure for 'operating profit before acquisition-related transaction and integration costs' for the following reasons:

(a) the lack of a definition of 'operating profit' before the finalisation of the General Presentation and Disclosures standard, as well as the lack of definition for 'integration costs';

(b) the PPA can be a lengthy process and therefore a reliable estimate of the depreciation related to the fair value adjustments may not be available in time for the first financial statements;

(c) the disclosure is only required in the year of acquisition and where the integration takes a longer period, the information in the year of acquisition would lack predictive value. Therefore, the benefits are unlikely to outweigh the costs. This expense could also be provided in the notes or another subtotal may be more efficient.

The respondent disagrees about the proposed disclosure about 'cash flows from operating activities' as this may be difficult to provide for the period before the acquisition and therefore do not consider that the benefits would exceed the benefits. With regard to the disclosure of cash flows from operating activities after the acquisition, the costs may exceed the benefits if the acquiree is fully and quickly integrated into the purchaser's operations.

299 Another respondent agrees with retaining the existing information. However, the respondent considers it not a priority for the IASB to develop guidance in this regard as it could be misleading as it would not be able cover all aspects and details for all industries. Entities should rather develop accounting policies in this regard and disclose these. The respondent would also agree with replacing 'profit or loss' with 'operating profit' as defined in the *General Presentation and Disclosures* ED.

300 One respondent disagrees with replacing profit or loss with operating profit before acquisition-related transaction and integration costs. They disagree with additional guidance but agree with keeping the existing requirements even if they have

[2] Such as in the Commission Regulation 809/2004 in the European Union.

reservations about the comparability and reliability of the proforma information. IFRS 3 paragraph B66 could be used to remove unnecessary requirements. To improve the comparability and understandability, the IASB may consider excluding the purchase price allocation adjustments from the proforma information, but this would require a significant change to the principles in IFRS 3.

301 Another standard setter observed that the demand for the proforma information is low and comparability across entities impaired, but they consider the existing requirements should be retained. However, it should be limited to transactions monitored by the CODM. They disagree with the development of guidance, but favour disclosure about the basis of preparation. The respondent also considers the terminology should be aligned with the ED *General Presentation and Disclosures* and that 'acquisition-related' and 'integration costs' should be defined. The respondent is also concerned that the cash flow information may not be available and would have to be collected manually at a high cost and while it may be useful information should be limited to transactions monitored by the CODM.

302 A standard setter agrees with the IASB proposals.

303 A standard setter agrees with EFRAG's response but notes that this question may be more relevant for users or preparers. Another standard setter considers that the pro forma information currently required by IFRS 3 is of little value to users and not used and therefore should be deleted.

304 Another respondent warns that the term proforma information could be confusing as this term is used in the context of prospectuses. The respondent agrees with the replacement of 'profit or loss' as proposed in the DP and recommended that definitions in IFRS 3 and the future replacement of IAS 1 are consistent. Lastly, the respondent suggested the issuance of additional guidance by the IASB on the following aspects:

(a) Should the financing of the transaction be considered?

(b) Should inter-company transactions be eliminated?

(c) How should accounting policy differences be treated?

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?

Proposals in the DP

305 *Many stakeholders have said that impairment losses on goodwill are sometimes recognised too late, long after the events that caused those losses.*

306 *The IASB identified two broad reasons for concerns about the possible delay in recognising impairment losses on goodwill:*

(a) *Management over-optimism—some stakeholders have concerns that management may sometimes be too optimistic in making the assumptions needed to carry out the impairment test.*

(b) *Shielding effect—a cash-generating unit, or group of cash-generating units, containing goodwill, typically contains headroom. Shielding arises because, applying current requirements, all reductions in total goodwill are allocated first to the unrecognised headroom. An impairment loss is recognised only when the recoverable amount of the cash generating unit falls below the carrying amount of the recognised assets and liabilities of the cash-generating unit. This means that a company recognises an impairment loss on acquired goodwill only once that headroom is reduced to zero. An acquisition could therefore underperform against management's expectations, but the company would recognise no impairment of acquired goodwill if it has sufficient headroom to absorb the reduction in value.*

307 *The IASB 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.*

308 *In doing so, the IASB investigated whether it could incorporate the estimate of headroom into the design of the impairment test, and by doing so:*

(a) *reduce the shielding effect;*

(b) *target the acquired goodwill more effectively; and*

(c) *require companies to recognise impairment losses on acquired goodwill on a more timely basis.*

309 *This 'headroom approach' would compare:*

(a) *the recoverable amount of the cash-generating units; with*

(b) *the sum of:*

(i) *the carrying amount of the recognised assets and liabilities of the cash-generating units; and*

(ii) *the headroom of the cash-generating units at the previous impairment testing date.*

310 *The IASB concluded that the 'headroom approach' would reduce shielding but not eliminate it, because:*

(a) *the allocation of any reduction in total goodwill is imperfect; and*

(b) *if the acquired business is performing poorly, better performance from other elements of the combined business could still shield the acquired goodwill from impairment.*

311 *Moreover, the 'headroom approach' could result in recognising impairments that are, in some circumstances, difficult to understand and the approach would increase cost.*

312 Because goodwill does not generate cash flows independently and cannot be measured directly, it must be tested for impairment with other assets. Thus, the IASB has concluded that some shielding is always likely to occur.

313 For the above reasons, the IASB's preliminary view is that it is not feasible to design a different impairment test that is significantly more effective than the impairment test in IAS 36 at recognising impairment losses on goodwill on a timely basis at a reasonable cost.

EFRAG's tentative position

EFRAG shares the IASB's reservations on the possibility to develop a different and more effective impairment approach. However, EFRAG believes that, without putting into question the fundamentals of impairment in IAS 36, there are collateral areas of possible improvements. EFRAG suggests that the guidance on goodwill allocation to cash generating units is discussed and possibly amended to improve how the test is applied in practice. In addition, better disclosures of estimates used to measure recoverable amounts of cash-generating units containing goodwill could supplement the improvements to goodwill allocation guidance. EFRAG seeks constituents' inputs on possible disclosure proposals to mitigate the risk of management over-optimism.

Summary of constituents' comments

314 The views provided differ mainly between preparers and other respondents like users, auditors and standard setters or regulators. While preparers are mainly reluctant to improve the guidance on allocation or reallocation of goodwill or to consider additional disclosures to make management overoptimism more transparent such proposals were appreciated by other groups of respondents.

Preparers

315 Preparers that provided a response agreed that developing a different and more effective impairment test would not be feasible at a reasonable cost.

316 A preparers organisation commenting was not aware of a lack of discipline in the application of impairment testing in practice. One preparer did not agree with the too late recognition of impairment losses criticism. A different preparers organisation regarded current impairment test as satisfactory. Opposite to that, from the perspective of an insurance preparers organisation the IASB's deep going analysis of the functionality of the impairment only approach provided an instructive evidence that it is defective and the losses on goodwill acquired are recognised far too late if any at all.

317 A preparers organisation commenting agreed that shielding is an aspect that could cause concern, but they considered this effect as a logical consequence of acquisition accounting. In their view this effect would be avoided if internally generated goodwill was recognised, though they were not convinced that this was something that the IASB should pursue.

318 A preparers organisation commenting considered that management optimism is an essential and natural aspect of human enterprise. The opposite, i.e., a pessimistic view could also be damaging to an entity's future. In their view, the COVID-related crisis was a good example of a situation where it would be overly pessimistic to write down goodwill on the basis of existing conditions at the end of the first or second quarter of 2020.

319 Another preparers organisation commenting shared the IASB's views that management over-optimism should be addressed by auditors and regulators. Another preparers organisation did not fully share this view but considered that any lack of discipline should be addressed by the auditors and not by increasing the disclosure burden.

320 A preparer expressed the view that management over-optimism in the impairment testing is not demonstrated as estimates are prepared and reviewed consistently with the company budget process, which involve control procedures. There are frequent analyses between forecast and actual data to ensure a good level of reliability of the estimates. They considered that a crisis should not immediately give rise to an impairment unless the acquirer expects that it would cause damages that would not be overcome in the future.

Improvement of guidance on allocation or reallocation of goodwill to CGUs

321 The few preparers that provided a response on this matter to EFRAG did not support the suggestion made by EFRAG that the guidance on the initial allocation of goodwill to CGUs as well as the guidance on the reallocation of goodwill based on the relative value approach should be further developed.

322 Some of the respondents argued that:

(a) Improving guidance on allocation and reallocation, making this a more 'rules-based' approach, seems contrary to IFRS principles based;

(b) Current IAS 36 guidelines are sufficient and enable the entity to use the judgement it deems relevant to enable a faithful representation of the transaction according to its facts and circumstances. The paragraphs 138 to 140 and 150 of the IAS 36 basis for conclusions provides useful guidance and the main issues with regards to the allocation and reallocation of goodwill to CGUs are already addressed; and

(c) "Shielding effect" is linked to the IASB's current conceptual view on goodwill, which is not to consider goodwill as a separate asset of the acquiree but rather as an asset representing the future economic benefits arising from other assets acquired in a business combination that are not individually identified and separately recognised. This asset relates to all the benefits that will be generated as a result of the integration of the acquisition within the group's businesses. This approach leads to allocating this asset to the CGU or the group of CGUs that will benefit from the acquisition, irrespective of whether other assets or liabilities of the acquiree are assigned to those units or groups of units. An inappropriate shielding effect would only occur in cases where the allocation of goodwill would not be made properly.

***Disclosures* to mitigate the risk of management over-optimism**

323 The few preparers that provided a response on this matter did not support the specific disclosures proposed by EFRAG to mitigate the risk of management over-optimism.

324 Some of the respondents argued that:

(a) These disclosures are difficult to prepare and highly sensitive information, therefore they would expect companies to be reluctant to provide the suggested disclosures. In addition, they noted somehow contradictory that some of the arguments used by certain stakeholders to place new disclosure requirements in the notes of the financial statements, in the sense that they could be more useful, have been disregarded in relation to over-optimistic projections within the impairment test; and

(b) Disclosing assumptions related to the period for which management has projected cash flows and the 'back-testing' disclosure could lead to wrong messages, should forecast not be reached. These are also commercially sensitive and the purpose of the financial statements is not to provide such disclosures. Likewise, providing information such as the current level of cash flows to allow users to model the future performance is not appropriate, as

external users would always miss some additional information to complete their projections in a reliable manner.

Other improvements

325 A preparer organisation from the banking industry highlighted that the cost of performing the impairment test was not proportionate to the importance of the information as given by financial analysts (according to its studies among 25% and 50% of the total accounting budget). In general, business analysts compare operational performance expectations with the actual value of capital stakes. Information of goodwill impairment is of limited use for this assessment. As such, goodwill is generally ignored by financial analysts. In addition, for financial institutions, capital regulations fully deduct goodwill from core capital as it is not considered a source of capital. Therefore, in its view efforts in preparing goodwill impairment tests exceeded decision usefulness. To reduce the cost of impairment test they provided the following proposals:

(a) Allowing/requiring amortisation of goodwill;

(b) Limiting impairment test to when there would be an indication of impairment;

(c) Reducing the frequency of the impairment test;

(d) Requiring impairment only test when the book value of equity compared with the market capitalisation of the company would exceed a given threshold;

(e) Introducing a less prescriptive approach;

(f) Introducing a more standardised approach; and

(g) Clarifying the requirements. There is lack on guidance on the issue whether the total value of all CGUs of a publicly listed entity could exceed the market capitalisation of the entity (the same for a specific CGU, if applicable).

326 To make the impairment test more useful, this preparer organisation suggested to disclose total acquired and internally generated goodwill and the change in the value in use from one period to another split into significant components.

Users

327 A user organisation agreed that the impairment test was not working properly. This was perceived as not providing sufficient information. In addition, there was an issue with the timing of impairments as the share price of the company was not affected by an impairment announcement as this was already discounted in the share price.

328 Another user organisation considered that the only useful information concerning impairment tests is the disclosure of the assumptions underpinning the impairment test, such as long-term growth rates and cash flows. Having this information would allow users to determine if management is being too optimistic or not. The best way to address this issue was to improve disclosure on the expected benefits of an acquisition, as proposed in the DP.

Improvement of guidance on allocation or reallocation of goodwill to CGUs

329 A user organisation expressed the view that entities should be more transparent in allocating the goodwill over the different segments which would facilitate users to understand and better assess the shielding effect. Entities should also explain the reasons for an impairment.

Other improvements

330 Some members of a user organisation suggested that it would be more meaningful for the acquirer to assess the market value of the acquired business on an annual basis and compared it to the original transaction. Any loss in value would result in the goodwill being adjusted downward.

Auditors

331 Auditors agreed that it is not feasible to design a significantly more effective impairment test as part of this project which did not include a comprehensive revision of IAS 36. They did not consider feasible a direct testing for goodwill impairment because goodwill was residual and could not be measured separately from the business it relates to and because it was composed of acquired goodwill and internally generated goodwill that could not be separated. Therefore, they suggested the IASB to undertake a broader research on IAS 36, including a comprehensive review focusing on the CGU and impairment testing concept.

332 Auditors agreed that management over-optimism and 'shielding effect' are important reasons affecting the recognition of impairments. Even though 'shielding effect' could not be completely avoided due to the CGU concept and the indirect testing, there were different aspects to be considered concerning "too optimistic" estimates. These include the inherent estimation uncertainty, the incentive effect of the business plan, management bias, window dressing, and the key significance of the last planning period for the terminal value cash flow.

333 Auditors did not share the IASB's view that over-optimism should only be dealt with by auditors and regulators because different aspects of over-optimistic estimates are also the responsibility of preparers (see paragraph 332). In addition, there was information asymmetry between the parties which usually does not allow enforceable corrections to a business plan beyond technical or obvious mistakes.

Improvement of guidance on allocation or reallocation of goodwill to CGUs

334 Auditors would appreciate more guidance on identifying CGUs and on allocating goodwill to CGUs, as indicated in paragraph 4.55 d) of the DP. This would improve the effectiveness of the impairment test. To this end, they suggested leveraging the proposed disclosures on synergies for also refining the requirements for goodwill allocation to CGUs.

Disclosures to mitigate the risk of management over-optimism

335 In relation to the specific disclosures proposed by EFRAG to mitigate the risk of management over-optimism, auditors considered that these are mainly implementation issues which should be addressed by better application rather by standard setting.

Standard setters and regulators

336 Standard setters that provided a response agreed that it would not be feasible to design a significantly more effective impairment test at a reasonable cost.

337 Most of the standard setters and regulators that responded to this question agreed that too optimistic estimates and 'shielding effect' were the main reasons for not recognising impairment losses on goodwill on a timely basis.

338 One standard setter disagreed with the view that the 'too little too late' is a widespread issue. In its view the statement on a lack of timeliness needed to be further demonstrated with empirical evidence. It was not aware of this issue being significant in its jurisdiction.

339 The same standard setter is also unconvinced that management over-optimism is one of the root causes for that issue. It argued that:

(a) This bias may exist but, in its view, this is not a pervasive issue. Thinking that management over-optimism is likely to explain any delay in the recognition of impairment losses is a simplistic statement that would need to be demonstrated;

(b) Paragraph 34 of IAS 36[3], if properly applied, creates a disincentive to management over-optimism;

(c) Changes in the facts and circumstances may not be reflected in a timely basis in the cash flow projections, in particular when those changes result in a decrease in value. It acknowledges such delays might exit but reflecting immediately adverse events without further thought could be interpreted as 'management under-optimism'. In addition, when observing negative business variances, management would first consider undertaking remedial actions to fix the problem and then assess whether those actions are successful before adjusting, if needed, the cash flow projections;

(d) Judgements and estimates, which are part of IFRS Standards, provide useful information to users about how an entity's management views its business;

(e) Impairment test is generally subject to close oversight from their governance, auditors and regulators. The audit of goodwill is also a frequent key audit matter in auditors' reports. This oversight provides some assurance that entities apply properly the requirements in IFRS Standards; and

(f) In its jurisdiction, management's performance is often assessed on management's ability to meet the main objectives upon which business plans are predicated. The assessment of management's performance determines the level of their variable compensation. Therefore, the way entities monitor their management performance significantly balances the risk of management over-optimism.

340 Most of the standard setters that responded to this question did not share the IASB's view, that over-optimism should be dealt with by auditors and regulators. They argued that:

(a) There is information asymmetry between the parties which usually does not allow enforceable corrections to a business plan beyond technical or obvious mistakes;

(b) The standard is too ambiguous and allows management to be over-optimistic while complying with it. Therefore, it is difficult for regulators to tackle management over-optimism; and

(c) The primary responsibility rest with the IASB in developing requirements that meet the test of demonstrating that they are capable of being applied faithfully and appropriately. The IASB would therefore be better advised to take on the challenge and think about suitable alternatives, rather than to hold on to an accounting construct that has proven not to be effective when it matters.

341 One standard setter considered that addressing management over-optimism is a prominent part of an audit and therefore they did not favour changing the accounting standard to address management over-optimism. Another considered that, in addition to over-optimism, shielding is best addressed by auditors and regulators.

342 The few standard setters that provided a response to EFRAGs question did not consider it is necessary to introduce consequences, as discussed in paragraph 120 of EFRAG DCL, for those companies that are generally over-optimistic.

---

[3] *IAS 36.34 Management assesses the reasonableness of the assumptions on which its current cash flow projections are based by examining the causes of differences between past cash flow projections and actual cash flows. Management shall ensure that the assumptions on which its current cash flow projections are based are consistent with past actual outcomes, provided the effects of subsequent events or circumstances that did not exist when those actual cash flows were generated make this appropriate.*

Improvement of guidance on allocation or reallocation of goodwill to CGUs

343 A majority of the standard setter and regulators agreed with EFRAG that the guidance on the allocation and reallocation of goodwill in CGUs could be improved as this could reduce shielding to a certain extent and reduce the judgment currently allowed in (re) allocating goodwill to CGUs. In this respect, they considered that the following specific improvements could be made:

(a) Develop application guidance on the requirements in paragraphs 80-87 of IAS 36. Paragraph 80 of IAS 36 required an entity to allocate goodwill to a unit or group of units that represent the lowest level within an entity at which the goodwill is monitored for internal management purposes and is not larger than an operating segment. However, no detailed application guidance supplemented this principle;

(b) Existing requirements exclusively rely on the level at which goodwill is monitored. The IASB should explore requiring entities to make more granular allocations of goodwill. (For example, test goodwill at the level at which synergies are expected to be realized or at a level that is consistent with the objectives initially set to assess whether that acquisition is performing as expected);

(c) To develop guidance for companies not listed and therefore not obliged to follow IFRS 8;

(d) Requiring an allocation of goodwill and therefore the impairment test at a lower level than currently required by IAS 36 paragraph 80, in particular if the test is done at operating segment level. Also providing more guidance on how to determine the relevant level of goodwill allocation. In addition, explaining what is meant by “benefit from synergies” and “monitoring of goodwill” and in what circumstances goodwill can be allocated at a level which is higher than the CGU would be helpful as it could make the testing more disciplined; and

(e) IAS 36 can be improved by amending the current principles for goodwill allocation to CGUs, such that goodwill is allocated to the lowest level possible that outweighs cost of impairment testing and information needs. In addition, allocation of goodwill needs to be better aligned with the way the (acquired) business is monitored by management in practice. This could mean that a critical assessment of the determination of a (group of) CGUs is needed. This also questions whether the operating segment level of IFRS 8 as used in IAS 36 is still appropriate. In this respondent’s view the referred operating segment level of IFRS 8 causes the level of allocation of goodwill being too high. The allocation of goodwill must be reliably determined in such a way that it is also verifiable for auditors.

Disclosures to mitigate the risk of management over-optimism

344 In relation to the specific disclosures proposed by EFRAG to mitigate the risk of management over-optimism, a few standard setters provided the following views:

(a) Disclosing additional information about the cash flow estimates would be relevant and useful to reduce overoptimism as it makes optimistic deviations more evident. Disclosing ‘back-testing’ information would improve transparency and it could also serve to make assumptions more realistic. Disclosing current level of cash flows provides information that is not directly comparable among entities and may not be useful. In addition, it could be sensitive information. Practice shows that the information disclosed by companies in the impairment section of the notes is scarce and trusting all the improvement to disclosures seems very optimistic;

(b) The IASB could investigate providing further clarity on how entities estimate terminal values and could develop disclosure requirements in addition to those in paragraph 134 of IAS 36. Such disclosures would help users understand the methodology and main inputs an entity has retained to determine terminal value as it accounts for a significant part of the value in use entities estimate;

(c) Management estimates have to be optimistic and the accounting rules should not make pressures in a different way; and

(d) It has reservations about the suggestions proposed by EFRAG. It is not convinced that accounting principles need to be developed to address management-over optimism. However, it recommends the IASB to investigate whether relevant assumptions about acquisitions, which provide useful information, could be considered to be disclosed.

Other improvements

345 Standard setter and regulators suggested further improvements to those mentioned in paragraphs 343 and 344:

(a) Should amortisation of goodwill be reintroduced a standard setter suggested the IASB considered a different approach (different that the one supported by IAS 36) with a simpler yet still justifiable methodology. The key logic of that test borrowed on the same rationale as for implied goodwill. The amount of the write-down was determined by comparing the fair value of the investment in the subsidiary with the total of the carrying amount of the net assets of the subsidiary in the consolidated financial statements and the net carrying amount of goodwill;

(b) The existing requirement in paragraph 124 of IAS 36 to not reverse an impairment loss for goodwill may adversely affect the timeliness of impairment. It thinks that permitting the reversal of an impairment loss for goodwill could be justified in some limited circumstances, when strong evidence exists that such reversal would not lead to the recognition of internally generated goodwill. This could be the case when the reversal occurs rapidly after the initial recognition of the impairment loss (for example, before the end of the following accounting period) and is linked to the correction of over-pessimistic cash flows projections due to circumstances independent of the entity's management;

(c) Components of goodwill that relates to a particular legal entity, such as deferred-tax-goodwill ("Technical goodwill") and employees should be kept at that entity level for impairment testing purposes;

(d) Providing further guidance to ensure that CGUs are set at the right level. It would be helpful for the IASB to provide further guidance on the notion of 'largely independent' cash flows. In its view the standard does not sufficiently explain what it takes for cash flows to be independent. Additionally, the notion of 'independent' cash inflows is also used when determining whether an asset is a corporate asset. Further guidance on how to determine whether cash flows are independent could improve the identification of a corporate asset;

(e) Requiring that the parts of goodwill which are allocated to specific components related to certain events or with a definite useful life are identified and measured separately, and thereafter de-recognised when a certain event occurs or when the useful life ends (technical goodwill);

(f) Providing more guidance on what is a “reasonable and supportable” cash flow projection (IAS 36 paragraph 33).[4] IASB could explore providing further detailed guidance or additional requirements on matters such as expected link between cash flow predictions and external evidence, expected link between capital expenditures and revenues or margin forecasts, the types of risk that should be included in the discount rate and how to reflect the less optimistic scenarios in cash flow predictions; and

(g) Strengthening the disclosure requirements in IAS 36 paragraph 134 (i) and (ii). For example, The IASB could require further disclosure of the growth rate used in the projected period on which cash flow projections are based (sometimes a “hockey stick” growth is observed in the year before the terminal value is established) or clarify what are the consequences if the key metrics on management expectations on integration of new business are not met.

[4] Examples given: -the expected link between cash flow predictions and external evidence; for example, the IASB could provide guidance on the fact that revenue estimates higher than the industry average should normally be supported by convincing evidence, such as significant investments or would not be expected in a starting-up or declining phase of the entity’s business cycle;

-the expected link between capital expenditures and revenues / margin forecasts; for example, the IASB could provide guidance that an increase in revenue or margin forecasts should normally be supported by convincing evidence, such as a committed increase in capital expenditures;

-the types of risk that should be included in the discount rate; for example, should an execution risk premium be included in the cost of capital?

-how to reflect the less optimistic scenarios (i.e. downturn) in cash flow predictions, for example by requiring issuers to use a multi scenario model and calculate a weighted average of three case scenarios – for example, the worst, the base and the best-case scenarios.

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?

Proposals in the DP

346 Having concluded that the approach in IAS 36 for testing goodwill for impairment cannot be significantly improved at a reasonable cost, the IASB considered whether to develop a proposal to reintroduce amortisation of goodwill. This is because amortisation could:

(a) *take some pressure off the impairment test, which may make the impairment test easier and less costly to apply.*

(b) *provide a simple mechanism that targets the acquired goodwill directly. By reducing the carrying amount of acquired goodwill, amortisation might help resolve the concerns of those stakeholders who believe the carrying amount of goodwill can be overstated because of management over-optimism or because goodwill is not tested for impairment directly.*

347 The IASB considered whether reintroducing amortisation or retaining the impairment only model.

348 Proponents of reintroducing amortisation generally give one or more of the following arguments:

(a) *The Post-implementation Review (PIR) of IFRS 3 suggests that the impairment test is not working as the IASB intended (impairment losses are not recognised on a timely basis, limited information value, the impairment test is complex and costly to perform).*

(b) *Carrying amounts of goodwill are overstated and, as a result, a company's management is not held to account for its acquisition decisions. Some argue that because goodwill can only be tested for impairment as part of a CGU, the resulting shielding by headroom causes too high a risk that carrying*

amounts of acquired goodwill could be overstated. Stakeholders with this view therefore argue the carrying amount of goodwill does not faithfully represent the future benefits still expected from the acquisition. Some stakeholders take the view that the impairment test is not effective at holding management to account for the significant amounts of goodwill recognised in acquisitions.

(c) *Goodwill is a wasting asset with a finite useful life, and amortisation would reflect the consumption of goodwill. Some argue that acquired goodwill is a wasting asset with a finite useful life. If acquired goodwill is consumed, investors would find it useful for the company to inform them about that consumption by recognising an amortisation expense in the income statement in the same period as the company obtains the benefits from consuming the goodwill.*

(d) *Amortisation would reduce the cost of accounting for goodwill.*

349 Proponents of retaining the impairment-only model generally give one or more of the following arguments:

(a) *The impairment-only model provides more useful information than amortisation. Some investors have said that amortisation expense provides investors with no useful information If determining the useful life of goodwill is arbitrary and the information provided by the impairment test is useful, even if it only has confirmatory value. Some also argue that amortisation of goodwill could make the information provided less useful. Amortisation could reduce the likelihood of an impairment loss being recognised because the reduction in carrying amount makes it less likely that the carrying amount would not be recoverable.*

(b) *If the test is performed well, it would be expected to meet its objective of ensuring that the carrying amount of acquired goodwill is recoverable from cash flows it is expected to generate jointly with other assets. The PIR of IFRS 3 and the IASB's subsequent research have not found new evidence that the test is not sufficiently robust. Some argue that the impairment test is working as the IASB intended when it designed the impairment test in 2004, because the IASB was already aware of the shielding effect.*

(c) *Acquired goodwill is not a wasting asset with a finite useful life, nor is it separable from goodwill subsequently generated internally. Some argue that companies acquiring businesses do so with the expectation that the acquired goodwill will be maintained indefinitely. They consider that some elements of goodwill have indefinite useful life, for example:*

(i) *cost savings that are expected to be recurring; and*

(ii) *the knowledge and processes to generate future returns beyond the timeframe of the recognised assets of the business.*

(d) *Reintroducing amortisation would not save significant cost because it would not eliminate the need for impairment testing.*

350 There are different views on whether there is a sufficient reason to change. Different IASB members place different weight on different arguments. Some of the main arguments IASB members considered in reaching their views were as follows:

(a) *Those who favoured reintroducing amortisation argued that:*

(i) *It has not proved feasible to design an impairment test that is significantly more effective at recognising impairment losses on goodwill on a timely basis. In their view, the IASB should reintroduce amortisation to respond to the PIR of IFRS 3 feedback that the impairment test is not*

robust enough to recognise impairment losses on goodwill on a timely basis.

(ii) *Carrying amounts of goodwill around the world have been increasing. Some IASB members see this as evidence that without amortisation management is not being properly held to account for its acquisition decisions and that amortisation is needed to maintain the integrity and reputation of financial reporting.*

(iii) *Goodwill is a wasting asset with a finite useful life, and reintroducing amortisation is the only way to depict that goodwill is being consumed.*

(b) *Those who favoured retaining the impairment-only approach argued that:*

(i) *Although the impairment test does not test goodwill directly, recognising an impairment loss provides important confirmatory information, even if delayed, that confirms investors' earlier assessments that those losses have occurred, helping hold management to account. The useful life of goodwill cannot be estimated, so any amortisation expense would be arbitrary. Therefore, investors would ignore it and amortisation could not be used to hold management to account for its acquisition decisions.*

(ii) *The IASB should not reintroduce amortisation solely because of concerns that the impairment test is not being applied rigorously or simply to reduce goodwill carrying amounts. In the view of some IASB members, goodwill could be increasing for many reasons—for example, because of the changing nature of the economy and greater value being generated by unrecognised intangible assets.*

(iii) *The IASB has no compelling evidence that amortising goodwill would significantly improve the information provided to investors or, particularly in the first few years after an acquisition, significantly reduce the cost of performing the impairment test.*

351 A small majority (eight out of fourteen IASB members) reached a preliminary view that the IASB should retain the impairment-only model. The IASB accepts that both accounting models for goodwill have limitations. The IASB reached a preliminary view that it should retain an impairment only approach, but this was by a small majority and so the IASB would particularly like stakeholders' views on this topic.

352 The IASB would especially welcome feedback that helps it understand:

(a) *why stakeholders have concerns that recognition of impairment losses on goodwill is not timely, and whether amortisation could and should resolve those concerns; and*

(b) *what information best helps investors to hold companies' management accountable for acquisition decisions at a reasonable cost.*

353 If the IASB decides to reintroduce amortisation, it will need to consider more detailed topics, including how should the useful life of goodwill and its amortisation pattern be determined.

354 The IASB has also considered and rejected two other approaches for accounting for goodwill:

(a) *immediate write-off of goodwill; and*

(b) *separating goodwill into components and accounting for the components separately.*

EFRAG's tentative position

EFRAG has not yet formed a view on whether amortisation of goodwill should be reintroduced, in combination with an impairment requirement, or whether no major changes to the current accounting for goodwill is justified. EFRAG is seeking views from its constituents and would welcome in particular new evidence, new arguments or new assessment on the existing evidence to support a change.

Summary of constituents' comments

355 15 out of 23 respondents representing national standard setters, preparers and users were in favour (or with majority of views in favour) of reintroduction of goodwill amortisation. These respondents were of view that impairment model was not working as intended and cannot be improved at a reasonable cost and therefore amortisation was a practical solution. From conceptual point of view, they considered goodwill to be a wasting asset which should be amortised to reflect its consumption.

356 Three respondents, standard setter and two user organisations were in favour (or with majority of views in favour) of keeping the existing impairment model on the grounds that the impairment test was the only conceptually correct model, that problems lied within its application and that it provided relevant and useful information to users and investors. These respondents also considered that no new arguments were provided to justify a change. In their view the impairment model worked as intended and no significant facts or circumstances were identified that would lead to reconsider the conceptual argument.

Four respondents representing preparers', professional organisations, and national standard setter, did not express a view, mentioning that both approaches had their advantages and disadvantages and absence of the new compelling evidence to support one of them.

357 One respondent proposed an accounting policy choice between amortisation and impairment options with disclosures of the rationale of this choice.

358 However, another respondent was against the accounting policy choice option due to the resultant lack of comparability between the companies and the impracticability of a reconciliation of the amounts to their respective alternative.

359 Another respondent with a majority of views for amortisation, suggested to apply a rebuttable presumption that acquired goodwill has a finite useful life which the entity can estimate sufficiently reliably and to amortise goodwill over this period. Where the entity can demonstrate on a continual basis that goodwill has an indefinite useful life, or that the useful life cannot be estimated reliably, the entity should be required to apply an "impairment-only" approach as at present. This approach would be consistent with that of IAS 38 for certain other intangible assets.

360 One respondent, a preparers' organisation representing financial institutions, noted that per the current prudential treatment goodwill was deducted from CET1 capital and therefore no difference in the solvency of the banking sector could be expected if the current impairment only model was replaced. If amortisation were to be reintroduced, this respondent would favour a retrospective application aligned with some local GAAP already applied to separate financial statements to achieve consistency and improve comparability.

361 One of respondents that did not express its position on amortisation, was of the view that the DP provided very few conceptual arguments of weight and did not develop adequately those that it presented, whether they be in favour of, or against, amortisation, and found this regrettable in a document Intended to aid reflection and discussion.

362 One respondent that was against the reintroduction of amortisation, was also not supportive of the model consisting in amortising *and* testing goodwill for impairment as it found the conceptual and practical arguments not convincing. This respondent also considered that entities will not achieve significant cost-savings if they would still need to perform an impairment test in addition to amortising goodwill.

363 Another respondent in favour of amortisation, suggested that if an impairment only model would be continued, certain items currently included in goodwill (e.g., technical goodwill related to the nominal deferred tax liabilities incurred in acquisitions) should be separated out of goodwill and allocated to profit or loss in the same period as the tax is settled.

Arguments for reintroduction of amortisation

364 Among others, the following arguments were presented by proponents of the amortisation model:

(a) Goodwill is a wasting asset and the amortisation would reflect goodwill consumption and take the pressure away from impairment test which could then be simplified. It is also a practical solution that targets goodwill directly unlikely to impairment test.

(b) The amortisation represents a mechanism to eliminate goodwill balances from the balance sheet when they are no longer reflective of the incremental value of the acquired business that was valid at the point of acquisition. Therefore, any sudden and material goodwill impairment charges (e.g., when the forward-looking information no longer supports the value) might not represent useful information in the P&L, particularly if they are applied to a value that has been outstanding on the balance sheet for a long time and thus already has limited predictive value.

(c) The amortisation represents a more pragmatic, cost-effective and standardised convention for the subsequent accounting for goodwill. Amortisation would mitigate the effects of shielding and management over-optimism and likely reduce the magnitude of any necessary impairments and could therefore take significant pressure off the impairment test itself.

(d) The amortisation expresses the return on investment within a limited time period that can be measured with an amortisation plan.

(e) The amortisation regime provides the necessary discipline which will create the reliable basis to provide some relaxation and simplifications of the impairment testing as proposed in the DP.

(f) When the amortisation charges are not included on an ongoing basis within the profit or loss account it creates an accounting incentive for M&A activities, potentially with significant overpayments. When the amortisation expense is included on a systematic basis in the income statement, it would hold management to account and it would increase the related discipline in the step before the acquisition decision is ultimately taken. The main reason is that most variable management compensations used to be earnings-based in practice.

(g) The results of recent studies[5] and research suggest that the impairment-only model does not reflect the economic life of goodwill. They showed that the implicit lifetime of goodwill in several studies reaches 100 years and more. On the other hand, empirical evidence shows that the association between

---

[5] Patloch-Kofler and Roider (2020), ASBJ and HKICPA Staff paper (ASAF meeting, April 2020, AP 1A); Bugeja and Gallery (2006), Ojala et al (2007)

goodwill and firm value and the value relevance of goodwill is decreasing very fast. The studies also showed that the impairment-only model offers a wide range of discretionary powers for goodwill accounting that is often – at least to some extent – utilised for earnings management. Disregarding these empirical results from the studies and observations and continuing not to amortise goodwill but instead account for it to infinity fails to meet the basic requirement of providing relevant information that is useful for economic decision-making.

(h) The amortisation would allow not to separately recognise the intangible assets like customer lists with finite useful lives, which would be subsumed in goodwill and amortised.

(i) The research conducted to date showed that little impairment was recorded in adverse market situations, therefore the was little correlation of a negative market situation and a decrease of fair value of CGUs. In addition, in most cases the share price of the company was not affected by the announcement of an impairment as the market had already discounted the adjustment in the share price before.

(j) The deficiencies revealed in the application of IFRS 3 could by themselves justify the reintroduction of amortisation, since after seeking the solutions, none have been obtained that can resolve the shortcomings that have arisen in the application of the impairment-only model. The reintroduction of goodwill amortisation is necessary to "maintain the integrity and reputation of financial reporting".

(k) Scepticism that the existing impairment-only approach should remain unchanged and that improvements to disclosures (although very important) could suffice, because these alone cannot address the existing shortcomings, acknowledged by the DP itself.

(l) The impairment test is insufficiently robust to measure any decline in the value of goodwill with a reasonable degree of reliability and objectivity;

(m) The existing impairment-only model is not sufficiently enforceable and auditable.

(n) The amortisation eliminates the differences between acquired goodwill, recognised on the balance sheet and internally generated goodwill. In the long run the acquired goodwill mixes with internally generated goodwill which implies this acquired goodwill should decrease over time.

(o) The amortisation model would improve the comparability between companies growing organically and by acquisition. The impairment model gives accounting incentives to the companies growing by acquisition and results in a significant increase in the amounts of goodwill recognised in balance sheets. The impact of the 'too little and too late' phenomenon might in consequence lead to significant pro-cyclical effects contradicting the political goal of stable economic growth.

(p) The non-amortisation of goodwill resulted in companies reporting inflated shareholder equity causing analysts to no longer use some financial ratios such as the net debt/equity ratio, a key measure for assessing the financial strength of a group. This ratio, when computed properly becomes an important indicator of the relative amount of money at risk by capital providers and bondholders.

(q) The regulators in banking and insurance sectors already disregard goodwill balances for prudential capital adequacy purposes (CRD IV and Solvency II frameworks). The reintroduction of amortisation would significantly reduce the compliance costs, efforts of statutory auditors and of enforcement authorities.

(r) Impairment is often seen as an acquisition failure; with the amortisation this perception could be less pessimistic.

(s) New evidence with regards to the possible functioning / misfunctioning of the existing impairment-only model could arise from the ongoing COVID-19 pandemic and from observing whether it will have an impact on the recognition of goodwill impairments in industries strongly impacted by the crisis. In that regard, the IASB could also assess whether the existing impairment-only model might have an impact for the stability of financial markets in light of its possible pro-cyclicality.

365 The majority of proponents of amortisation suggested that the amortisation model should be accompanied by either annual quantitative or indicator-only impairment test.

Arguments against reintroduction of amortisation

366 Among others, the following arguments were presented proponents of impairment model:

(a) Goodwill is not a wasting asset. If the business combination is successful, the value of the goodwill could rise, and the business acquired could even be sold at a higher price;

(b) Goodwill is neither a wasting asset with a finite useful life nor an accounting construct but, on the contrary, a genuine "asset representing the future economic benefits arising from other assets acquired in a business combination that are not individually identified and separately recognised" (IFRS 3). It is therefore not possible to predict either the useful life of acquired goodwill or an amortisation pattern, unlike other intangible and tangible assets, and this makes any amortisation charge at best completely arbitrary, and likewise also the remaining balance sheet value;

(c) Goodwill is part of the acquisition price paid and is therefore an indicator for the value of the future free operating cash flows (at least seen through the eyes of the acquirer). Goodwill is an asset, is part of "invested capital" and determines thus whether a reporting entity is profitable or not.

(d) Any goodwill amortisation charge is the result of spreading the cost of something that cannot be directly measured over a highly subjective period of time with no cash flow implications.

(e) 'Too little too late' is not an issue pervasive enough to trigger a change in the accounting for goodwill and there is no evidence at this stage to conclude that the test fails to provide timely information;

(f) Management judgements and estimates provide useful information to users about how an entity's management views its business and how it thinks business will unfold—this should not be conflated with management's bias and overoptimism;

(g) The entity does not have to replace the goodwill after the so-called useful life period as with other type of assets (e.g., production facilities). Hence, the entity does not have to recover the cost of the goodwill;

(h) Goodwill does not lose value in the same way as other assets. Instead, it does so because of individual events, and these are better reflected as impairment charges, e.g., changes in the business environment, for which impairment charges better reflect the economic reality; and/or and failures of management, for which impairment charges better reflect the stewardship/ accountability objective of financial reporting. These kinds of signals to capital markets have substantial micro-and macro-economic benefits;

(i) An impairment charge should be an indicator, to the extent that the financial markets have not yet discovered the problem, that the acquisition was overpaid, i.e., that the free operating cash flows do not live up to the expectations.

(j) If goodwill is reduced in value by arbitrary amortisation over time, the value of an impairment charge will only partially reflect the impairment event itself. This conveys less relevant information to the investors, and it provides a poorer basis for management to be accountable;

(k) Amortisation expense would represent an arbitrary figure in P&L that would not represent a useful performance indicator and that would create unnecessary volatility in the income statement.

(l) The amortisation expense will provide little if any relevel information to users and would fail to provide information whether an acquisition was successful which is inconsistent with the objective of the IASB project;

(m) The cessation of amortisation at the end of the economic life of goodwill can lead to a significant step-up in net profit which is difficult to link to a real economic event.

(n) Preparers, auditors and users have got used to the existing treatment of goodwill, and any changes to this are likely to be costly. No cost-benefit analysis of the switch to amortisation has been carried out.

(o) The implications and cost of the reintroduction of amortisation may be so important that the threshold to make that accounting change would be very high. Practical arguments supporting amortisation are unlikely, alone, to exceed that threshold.

Useful life and amortisation pattern

367 Ten respondents considered that management could estimate the useful life based on a goodwill consumption pattern, the payback period of the investment and the amortisation pattern - on the basis of the realisation of the expected synergies. They considered that the determination of useful life of goodwill was not more complex than for any other tangible or intangible asset and could be revised if circumstances change. They also suggested that accounting standard could set a predetermined maximum as a rebuttable presumption (e.g., 10 years as in the EU accounting directive), if the useful life cannot be reliably estimated in particular circumstances.

368 One respondent observed that the European entities that apply the accounting directives amortise goodwill and also the entities that apply the IFRS for SMEs amortise goodwill. Therefore, a relevant number of entities already amortise goodwill and estimate in a reasonable way its useful life. There is an experience in applying National GAAP that could be shared with the IASB.

369 One respondent asked for clarification whether the useful life period would be set by the IASB or by companies themselves.

370 One respondent suggested to use a multiple such as price / current earnings (or price / expected earnings) as an estimate of the useful life of goodwill.

371 The amortisation pattern to be applied should be based on a judgment by the companies and one could also assess whether goodwill can be split into different components that have different useful lives.

372 Four respondents, suggested to introduce a straight-line amortisation as a pragmatic, transparent and cost-effective solution which contributes to more robustness of balance sheets at micro basis and financial stability at macro level.

373 One respondent suggested the IASB to specify the transition requirements, for example whether the amortisation should be applied prospectively or retrospectively.

374 One respondent suggested that the goodwill amortisation should not be done on the basis of an arbitrary and uniform amortisation period. As far as possible useful lives should reflect the economic environment of the entity and the specific circumstances and attributes of each acquisition.

Would a new MPM be created to add back the amortisation expense?

375 One respondent considered that a new MPM would probably not be created since the profit or loss impact of the amortisation was less discretionary, more homogeneous over time and was known from the moment of acquisition.

376 One respondent had no firm indication whether amortisation would be adjusted out in management performance measures but assumed that fewer users would adjust out such an amortisation expense than the current goodwill impairment charge. This is because the periodic amortisation expense would reflect (although rather arbitrary) the cost connected to a wasting asset (goodwill), while currently the impairment charge is not considered to be part of the performance/result for the period.

377 Three respondents considered that financial analysts are likely to add amortisation expense back for the purpose of forecasting company earnings and cash flows, in the same way it is currently done for impairments.

Age of goodwill

378 Two respondents considered it useful as it would provide relevant information to users.

379 Another respondent, more particularly the members who did not support the reintroduction of goodwill amortisation, did not agree with a specific requirement to disclose information about the 'age' of goodwill. In this member view, it would simply be misleading, where useful lives cannot be determined.

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?

Proposals in the DP

380 The IASB's preliminary view is that it should develop a proposal to help investors better understand companies' financial positions by requiring companies to present on their balance sheets the amount of total equity excluding goodwill. The IASB reached this view because it was considered that:

(a) *Goodwill is different from other assets with a unique nature.*

(b) *Presenting this amount could help to highlight those companies for which goodwill is a significant portion of their total equity.*

381 Presenting total equity excluding goodwill as a subtotal within the structure of the balance sheet could highlight the subtotal's relationship with other items in the financial statements. However, changing the structure of the financial statements to

allow the presentation of this subtotal could be too disruptive. Therefore, the IASB does not intend to pursue such a change and companies would present this amount as a free-standing item.

EFRAG's tentative position

EFRAG does not support the IASB's proposal to require companies to present on their balance sheets the amount of total equity excluding goodwill.

Summary of constituents' comments

No support for companies to present on their balance sheets the amount of total equity excluding goodwill

382 Almost all respondents did not support the IASB's proposal to require companies to present on their balance sheets the amount of total equity excluding goodwill.

383 Some of these respondents argued that:

(a) this would contradict the recognition of goodwill as an asset. In particular, subtracting goodwill from equity might suggest that goodwill is not a "reliable" asset when compared to other assets, contradicting the accounting and casting further doubt on the reliability and usefulness of the impairment test;

(b) the figure can be computed easily, especially when considering the proposals under the IASB's Exposure Draft *General Presentation and Disclosures*, which proposes that goodwill shall be required to be presented as a separate line item in the balance sheet;

(c) the IASB's proposal would be more harmful and misleading than beneficial and expressed concerns on how the resulting (artificial) figure will interpreted;

(d) such presentation could raise (legal) questions for financial agreements including financial covenants; and

(e) presenting the amount of total equity excluding goodwill, without disclosing whether part of the goodwill relates to non-controlling interests would be of little use.

384 Nonetheless, some of these respondents:

(a) suggested that such information could be useful within an 'illustrative note' (even though such calculation can be made by users of financial statements with the information already provided);

(b) suggested that if the IASB had doubts about the appropriateness of recognising goodwill as an asset, then it should be more direct in its approach and either reintroduce amortisation or require goodwill to be deducted from shareholders' funds; and

(c) supported presenting a single line item on Goodwill in the statement of financial position as proposed in the IASB's Exposure Draft *General Presentation and Disclosures*.

Support for companies to present on their balance sheets the amount of total equity excluding goodwill

385 One respondent supported the proposal for companies to present on their balance sheets the amount of total equity excluding goodwill as a freestanding information. This respondent agreed with the IASB rationale that it is essential to make even more transparent the unique nature of the goodwill asset as a residual item. It would be also in line with the prudence principle.

386 In addition, this respondent suggested that:

(a) if the impairment-only model is retained, the IASB should require that the weaknesses of the current goodwill accounting model by its design are prominently highlighted by reporting entities; and

(b) the IASB should reconsider the labelling of the residual item as currently the denomination “goodwill” is not fully reflecting the true nature of what it intends to faithfully represent. Hence, if the current accounting approach is retained and the immediate write-off is not an option a more prominent presentation of the residual item and its impact on equity is essential to be provided.

Other views

387 One respondent did not have strong views on the proposal to require disclosure of total equity excluding goodwill as a separate item in the balance sheet as a free-standing item as this new line item did not seem to solve any of the concerns raised on goodwill.

388 A user organisation had mixed views as some members consider that this disclosure would not benefit users as it re-classifies goodwill as an artificially created intangible and the metric can be recalculated easily. However, other members consider that the disclosure would display the quality of capital to users and act as a bulwark against the delayed recognition of impairment. Some members consider that indefinite lived intangibles should be included with goodwill in this disclosure.

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?

(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?

Proposals in the DP

389 Having reached the conclusion that it could not make the impairment test significantly more effective at recognising impairment losses on goodwill on a timely basis at a reasonable cost, the IASB investigated whether it could simplify the test without making it significantly less robust.

390 This section discusses the IASB’s preliminary view that it should develop proposals intended to make the impairment test less costly and less complex, while improving some aspects of the information it provides.

391 The IASB’s preliminary view is that it should develop a proposal to remove the requirement for a company to perform an annual impairment test for cash-generating units containing goodwill if there is no indication that the cash-generating units may be impaired. That proposal would also apply to intangible assets with indefinite useful lives and intangible assets not yet available for use. A company would still need to assess at the end of each reporting period whether there is any indication that there may be an impairment.

392 Some IASB members may be prepared to remove the requirement for an annual impairment test, but only if the IASB also reintroduces amortisation of goodwill. In

their view, reintroducing amortisation would reduce reliance on the impairment test and justify removing the requirement for an annual impairment test.

393 A narrow majority (eight out of fourteen IASB members) favour removing the requirement for an annual impairment test, even though the IASB's preliminary view is that it should not reintroduce amortisation. They agree that removing the requirement would make the test marginally less robust. However, they also consider that when the company has no indicator of impairment the benefits of testing for impairment are minimal and so do not justify the cost in those cases.

394 Because moving to an indicator-based approach would place more reliance on identifying indicators of impairment, the IASB plans to assess whether it needs to update the list of indicators in paragraph 12 of IAS 36.

EFRAG's tentative position

EFRAG has reservations in introducing an indicator-only approach.

Summary of constituents' comments

395 13 out of 20 respondents, represented by preparer organisations, professional organisation, regulator, national standard setters and user organisation, do not support the indicator-only approach. The respondents supporting consist of preparers, market organisation and national standard setters.

396 9 out of the 13 respondents who do not support the indicator-only approach, would support the indicator-only approach in combination with the reintroduction of the amortisation. The main argument is that the potential shortcomings of the indicator-only approach will be less relevant as the amortisation would reduce the pressure from the impairment test by reducing the potential overstatement in the carrying amount of goodwill. One national standard setter comments that if amortisation is not reintroduced, the annual impairment test should be retained as it is seen as part of the package when the impairment-only approach was introduced by the IASB.

397 A user organisation comments that the impairment test should remain, however a qualitative test should be sufficient when implemented under strict conditions if there is no indication that the goodwill will be impaired. There is also contend that the quantitative test should be applied on an annual basis and its methodology transparently disclosed. They also consider that the methodology and parameters used should be verifiable so it can be assessed if an entity is taking a realistic and reasonable approach to justify not performing the quantitative impairment test.

398 Another user goes even a step further. A majority of members suggest a way to reduce "the cost and complexity of performing the impairment test for goodwill, without making the information provided less useful to investors". From their view goodwill impairment has little or no practical value to equity investors as it will almost always be obvious long before the impairment that the premium paid was excessive.

Details to the constituents' comments

399 The arguments used by the two preparer organisations against the indicator-only approach are the following:

(a) The simplification is counterintuitive to the objective of the IASB's DP in trying to make the impairment test more effective and timely;

(b) The expertise of performing the impairment test will reduce and there will be no test available from the comparative period for benchmarking purposes if not performed regularly;

(c) The process of data collection and internal organisation around performing the quantitative test will be disrupted making the testing more complex;

(d) No significant cost savings expected from the indicator-only approach as the list with triggers in IAS 36 needs to be updated/extended and additional discussions with auditors/enforcers will occur to support the interpretation and the strength of the indicators;

(e) Any cost savings will not outweigh the negative impact due to loss of robustness and increased subjectivity; and

(f) The quantitative test would be continued as it will be required for internal control, managerial or assurance purposes.

400 One preparer organisation notes that the accounting approach for intangible assets with an indefinite useful life and intangible assets not yet ready for use should be the same as the accounting approach for goodwill, regardless of the accounting method elected.

401 Other respondents expressed the following arguments against the indicator-only approach:

(a) Useful information will be lost (e.g., regular disclosure of discount rates, growth rates and key assumptions).

(b) The simplification is counterintuitive to the objective of the IASB’s DP in trying to make the impairment test more effective and timely;

(c) The quantitative impairment test is an essential tool for auditors, enforcers and also for the Supervisory Board/Audit Committee to challenge the recoverable amount and therefore the management;

(d) The annual quantitative test prompt management to assess the cash generating process, promoting good stewardship;

(e) The indicator-only approach will not solve or even increase the 'too little too late' issue. The level of subjectivity will increase, in particular when operating performance is deteriorating slowly. The only difference with the quantitative test is that the focus moves from key assumptions in the impairment test to the triggers used in the indicator-only approach;

(f) Any proposals to simplify the impairment test without requiring the re-introduction of the amortisation of goodwill could increase the risk that impairment losses are not timely recognised;.

(g) The impairment test will become less robust due to loss of valuation expertise and more difficulty to assess reasonableness of the set of assumptions when the test is not performed for several years and will not be available for benchmarking; and

(h) The indicator-only approach might not lead to reduced cost, because:

(i) a robust and supportable analysis and documentation of qualitative triggers might be a costly exercise, especially in first periods and when considering additional assurance costs;

(ii) more robust triggers will have to be determined as the current triggers are not robust enough for the indicator-only approach while they are sufficient in combination with the annual quantitative test;

(iii) the disclosure requirements in paragraph 134 of IAS 36 will not be applicable if no quantitative test is performed, meaning that comprehensive new disclosures concerning the qualitative trigger testing would be reasonable and provide useful information; and

(iv) preparers need to continue monitoring the cash flows generated by the business as proposed in the IASB’s DP in relation to disclosing the subsequent performance of an acquisition.

402 Few respondents do not agree that the indicator-only approach will make the impairment test less robust if implemented:

(a) The increased management judgment can be solved by providing more application guidance on identification and use of indicators;

(b) The increased possibility for over-optimism can be solved by enhancing disclosure requirements informing users which and how indicators and assumptions are used by management; and

(c) The potential loss of expertise due to changes in teams is currently also applicable as teams are changing continuously due to natural turnover.

403 Some respondents additionally suggest to explore enhancing the current relief in IAS 36 paragraph 99 instead of developing an indicator-only approach. This approach could lower the cost without removing the quantitative impairment test. One preparer in favour of the indicator-only approach, also suggests to permit using the most recent detailed impairment test in current period provided all criteria are met, in case the indicator-only approach is not implemented.

404 The respondents in favour of the indicator-only approach, use the following arguments:

(a) The impairment test does not have added value when significant headroom is available;

(b) The indicator-only approach makes the impairment test simpler;

(c) The indicator-only approach is less costly and less time consuming, however the market organisation expects marginal cost savings since an assessment on the indicators is still necessary. One national standard setter emphasises the importance that the impairment test is retained regardless whether the amortisation is reintroduced;

(d) The indicator-only approach will not reduce the expertise either because the impairment test will continue to be performed for internal management reasons or because it is readily available; and

(e) The value of the (intangible) asset will be justified by performing an analysis of the performance of the CGU to identify triggers, just like currently done for individual fixed assets.

405 However, some respondents acknowledge that additional guidance on the identification and use of indicators is necessary to increase the robustness and discipline in case the indicator-only approach is implemented, and some suggest specific guidance:

(a) Additional disclosure requirements informing the users on the indicators used and the assumptions made by management, which should be more complete and specific than current requirement in paragraph 130(a) of IAS 36. This is in line with arguments that respondents use against the expectation that the indicator-only approach will result in cost reduction as presented in paragraph 401(h)(iii);

(b) The quantitative impairment test should be performed at acquisition date so users can use the inputs as reference in subsequent periods to determine if there is an indicator for impairment; and

(c) Removal of cash flows relating to a certain project from the VIU calculation should be added to the list of indicators.

406 One preparer supporting the indicator-only approach does not share the reservations of EFRAG on the indicator-only approach as they do not need to perform a goodwill impairment calculation for all CGUs to identify those for which

there is no indication of impairment. The preparer also suggests aligning the indicators with the US GAAP principles.

407 Another preparer organisation supporting the indicator-only approach notes that users should not use the metrics as proposed to be disclosed in the DP as an indication of impairment, since these have different objectives and should not be used as indicators for impairment.

408 Two preparer organisations in favour of the indicator-only approach emphasises that the cost of the proposed disclosure requirements relating to the subsequent performance of an acquisition outweighs the benefits (cost reduction) from the indicator-only approach. In particular because companies are expected to continue the quantitative impairment test as it is complex and regular testing guarantees more consistent and reliable results. One of the preparer organisations recommends that the disclosure requirement should only be mandatory when there is an indication for deterioration compared to initial expectations.

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.

Proposals in the DP

409 The IASB's preliminary view is that it should develop a proposal to remove from IAS 36 the restriction on including cash flows arising from a future restructuring to which a company is not yet committed or from improving or enhancing an asset's performance. This proposal would apply not only to cash-generating units containing goodwill but to all assets and cash-generating units within the scope of IAS 36. The IASB reached this view because it was considered that this approach will:

(a) *Reduce cost and complexity.*

(b) *Make the impairment test less prone to error because estimates of value in use would probably be based on cash flow projections which are prepared, monitored and used internally for decision-making regularly.*

(c) *Make the impairment test easier to understand.*

(d) *Make the impairment test easier to perform and therefore could make it easier to audit and enforce.*

410 Some argue that simply removing the restriction on these cash flows could increase the risk that management may use inputs that are too optimistic in estimating value in use. However, The IASB's preliminary view is that setting a probability threshold or requiring additional qualitative disclosures is unnecessary for these cash flows. These cash flows would still be subject to the same requirements that apply to all

cash flows included in estimates of value in use—companies would be required to use reasonable and supportable assumptions based on the most recent financial budgets or forecasts approved by management.

411 *In addition, the IASB's preliminary view is that it should develop a proposal to:*

(a) *Remove the explicit requirement to use pre-tax cash flows and pre-tax discount rates in estimating value in use.*

(b) *Require a company to use internally consistent assumptions for cash flows and discount rates regardless of whether value in use is estimated on a pre-tax or post-tax basis.*

(c) *Retain the requirement for companies to disclose the discount rates used but remove the requirement that the discount rate disclosed should be a pre-tax rate.*

412 *The IASB reached this preliminary view because it was considered that removing the requirement to use pre-tax cash flows and pre-tax discount rates would:*

(a) *Make the test easier to understand by aligning it with common valuation practice.*

(b) *Not require companies to calculate pre-tax discount rates solely to satisfy the disclosure requirements of IAS 36.*

(c) *Provide investors with more useful information, because companies generally use post-tax discount rates as an input in estimating value in use. The disclosure of a post-tax discount rate would be more useful information for investors than disclosure of a pre-tax discount rate, which generally is not understandable or observable.*

(d) *Better align value in use in IAS 36 with fair value in IFRS 13 Fair Value Measurement.*

(e) *Maintain consistency with an amendment made in 2008 to IAS 41 Agriculture (for the discount rate) and an amendment to IAS 41 (for cash flows) proposed in 2019*

413 *This proposal would apply not only to cash-generating units containing goodwill but to all assets and cash-generating units within the scope of IAS 36.*

414 *However, some stakeholders have concerns and questions about how to avoid double counting of future tax consequences.*

415 *The IASB in making a similar change to IAS 41 the IASB simply deleted 'pre-tax' and did not add any further guidance. The IASB intends to adopt the same approach in this case.*

EFRAG's tentative position

EFRAG supports the IASB' proposal to remove the restriction in IAS 36 that prohibits companies from including cash flows arising from a future uncommitted restructuring, or from improving or enhancing the asset's performance. However, additional guidance would be required on when to include restructuring cash flows in the calculation.

EFRAG supports the IASB' proposal to remove the explicit requirement to use pre-tax inputs and pre-tax discount rates to calculate value in use.

Summary of constituents' comments

Removing the restriction to include cash flows from future uncommitted restructurings and asset enhancements

416 17 out of 21 respondents represented by preparers, user organisation, professional organisation, market organisation and national standard setters, support this simplification. One national standard setter is concerned since the line between the FVLCD and VIU becomes unclear. One preparer, a regulator and one member of a bigger user organisation is against this simplification.

417 The respondents supporting this simplification use the following arguments:

(a) Reduces cost and complexity as it will be consistent with management assumptions in internal forecasts and budget exercises which are subject to management review and readily available.

However, one national standard setter notes that it is conceptually not in line with the VIU determination;

(b) Enhancements to asset performance has a direct effect on future cash flows and since goodwill represents the future expected cash flows, it is conceptually correct to include these in calculating the VIU;

(c) Aligning cash flows used in impairment testing and corporate planning documents will further enhance consistency with other information provided in for example the management commentary.

(d) A market participant would also take these cash flows into consideration when determining the maximum price to be paid. The VIU should approximate FVLCD since these CFs represent real value in management's view; and

(e) Uncertainty should not be a reason that withholds these CFs to be allowed as uncertainty is applicable to valuation of various assets and should be treated the same way for these CFs.

418 However, many of the respondents do suggest further considerations and require additional guidance regarding:

(a) More investigation needed to conclude which cash flows to permit and which are prohibited. One national standard setter specifically proposes the following scoping:

(i) exclude CFs from enhancements or improvements related to future business combinations even if these ultimately will be included in the existing CGU and business plans. In the future goodwill may be recognised due to these business combinations, therefore including the CFs when calculating VIU will be inconsistent;

(ii) include CFs from future operations that are expected to be implemented with a sufficient probability; and

(iii) include CFs from restructurings that meets or is expected to meet by the date of authorisation for issue of an entity's financial statements, all legal requirements for being announced to its employees. However, since impairment tests are often performed before the end of the reporting period, this could prove difficult to ascertain with an appropriate level of confidence. Furthermore, in the French jurisdiction there are legal requirements to inform/consult employees on any projected restructuring before announcing to general public. This may create practical/legal difficulties, leading entities to provide boilerplate information to comply with legal requirements.

(b) More guidance on the timing to include cash flows to avoid diversity and over-optimism in practice by aligning with IAS 37. The national standard setter refers to specific valuation guidance that has been developed in Austria and Germany, which is generally accepted and relevant for transaction and fair value calculation purposes and could therefore serve as a basis for market-proven guidelines. Some respondents note that such CFs should only be allowed if the plans are sufficiently detailed and approved at least by senior management to guarantee robustness by analogy to IAS 37 paragraph 71 and up;

(c) However, some respondents do not agree with additional thresholds to avoid over-optimism as current requirements in IAS 36 already require reasonable and supportable assumptions. Furthermore, internal processes for budgeting/forecasting are internally challenged and exposed to oversight from management. This view is supported by the professional organisation as IAS 36 already requires projections to be based on the most recent budgets approved by management; and

(d) The clarification of the scope of the current proposed simplification. The professional organisation interpret the current wording as more cash flows are permitted to be included but consider that some stakeholders could have a narrow-scoped interpretation limiting to only the cash flows mentioned in the proposal.

419 Some respondents do not support simplification using the following arguments:

(a) It increases the subjectivity of the VIU and risk of optimism even further;

(b) The cash flows included in the test should be based on plans and budgets approved by management. Including cash flows of restructuring initiatives that the management has not approved (and therefore the entity is not committed to) might make impairment tests overly optimistic, lacking documentability which makes it difficult to audit/enforce;

(c) Increases the shielding effect since future restructurings and asset enhancements create value which is unrelated to the original goodwill recognition; and

(d) The IASB's proposal may be conceptually problematic as the impairment test is required to test the value of the asset at the reporting date. By including uncommitted material restructurings, enhancements or improvements, the value of that asset is not tested at the reporting date, but it would be the value of a possible altered asset or group of assets at a future date. Planned improvements and enhancements may give rise to assets that would be separately recognised in the future in accordance with the appropriate standard (e.g., IAS 16). These future assets, once they are acquired, would be subsequently subject to measurement themselves (i.e., impairment testing).

420 One preparer organisation supports applying this simplification to other fixed assets. A national standard setter prefers a generic principle applicable to a broader range of CFs.

Removing the restriction to use post-tax cash flows and post-tax discount rates

421 21 out of 22 respondents represented by preparers, user organisation, professional organisation, market organisation, regulator and national standard seters support this simplification. However, one of the respondents generally supports the simplification but questions simplification as it seems to bring more complexity.

422 The following arguments are used to support this simplification:

(a) Using pre-tax input is not feasible;

(b) From an operational perspective currently pre-tax rates are already derived from post-tax cash flows;

(c) Aligns with commonly used valuation methodology for example the WACC is used for discounting which is a typical post-tax measure making the test simpler;

(d) Better represents future cash flows from the business combination and harmonises the VIU calculation method and the FVLCD which is conceptually sound;

(e) Will be more in line with management estimates which are readily available making it less costly and complex reducing also the susceptibility for errors; and

(f) Consistency between rates and inputs used would be required without demanding more requirements.

423 Some respondents suggest specifying the meaning of post-tax to avoid diversity in practice (e.g., IAS 12.24 concerning the treatment of deferred tax assets on tax loss carry forwards in the impairment test and IAS 12.53 concerning the prohibition of discounting the DTA while discounting is necessary for VIU). To this end a clarification will be necessary of how this proposal to include post-tax information aligns with IAS 12 Income Taxes. In addition, one national standard setter expects that the IASB should solve the issue relating to what tax attributes should be reflected in the VIU as discussed in paragraphs BC93 and BCZ81-BCZ84 of IAS 36 or explain why it is not relevant anymore.

424 The preparer organisation considers additional discipline on the simplification to be inappropriate and unnecessary. However, other preparers would not disagree with further guidance to avoid double counting of tax cash flows in estimating VIU. However, one national standard setter supports additional guidance to ensure that post-tax calculation is consistent and comparable in practice.

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?

Proposals in the DP

425 The IASB considered whether to provide the following simplifications and guidance for the impairment test:

(a) *Adding more guidance on the difference between entity specific inputs used in value in use and market participant inputs used in fair value less costs of disposal.*

(b) *Mandating only one method for estimating the recoverable amount of an asset (either value in use or fair value less costs of disposal) or requiring a company to select the method that reflects the way the company expects to recover an asset.*

(c) *Allowing companies to test goodwill at the entity level or at the level of reportable segments rather than requiring companies to allocate goodwill to*

groups of cash-generating units that represent the lowest level at which the goodwill is monitored for internal management purposes.

(d) *Adding guidance on identifying cash-generating units and on allocating goodwill to cash-generating units.*

426 However, the IASB's preliminary view is that it should not develop proposals for any of these potential simplifications or guidance because:

(a) *The guidance in IAS 36 and IFRS 13 is sufficient.*

(b) *The IASB's reasons for basing the definition of recoverable amount on both value in use and fair value less costs of disposal when developing IAS 36 remain valid.*

(c) *Testing goodwill at a higher level could delay further the recognition of impairment losses of goodwill by increasing the effect of shielding.*

(d) *It would be difficult to provide guidance on identifying cash-generating units and allocating goodwill that could apply to all companies.*

EFRAG's tentative position

EFRAG supports the IASB's preliminary view to not develop the following proposals:

(a) Adding more guidance on the difference between entity-specific inputs used in value in use and market-participant inputs used in fair value less costs of disposal.

(b) Mandating only one method for estimating the recoverable amount of an asset or requiring a company to select the method that reflects the way the company expects to recover an asset.

(c) Allowing companies to test goodwill at the entity level or at the level of reportable segments.

However, EFRAG does not support the IASB's view to not add further guidance on allocating goodwill to cash-generating units.

Summary of constituents' comments

427 Many respondents agree with not developing further all or part of the simplifications as presented in the DP, some respondents argue that the too little too late problem might worsen due to further simplifications. Many respondents are opposed against the use of one method in calculating the recoverable amount and in particular opposed against the removal of VIU as it:

(a) Reflects the manner in which an entity expects to use an asset, independently from the view of market participants;

(b) Comparable valuation inputs are not always available for determining the fair value of CGUs. Therefore, the FVLCD will not be a solution for the over-optimism relating to the VIU since the FVLCD will not be based on observable prices leading to judgmental level 3 valuations; and

(c) One of the national standard setters notes that the arguments in paragraphs BCZ29-BCZ30 of IAS 36 are still applicable.

428 Many respondents do propose further simplifications:

(a) Support for further developing guidance on allocation of goodwill to CGUs as it would further simplify and improve the effectiveness of the impairment test. To this end, the professional organisation suggests leveraging the proposed disclosures on synergies for also refining the requirements for goodwill allocation to CGUs.

However, one preparer does not support to develop further guidance on allocating goodwill to CGUs. A preparer organisation argues that allocation of goodwill to a higher level is conceptually possible as the shielding effect is a feature of the correct assessment of the performance of an acquisition and therefore disagrees with the statement that goodwill should all allocated to a lower level, requesting more in-depth research and discussion. A national standard setter considers additional guidance on allocation not feasible due to wide variety of companies and different characteristics of acquisitions;

(b) Guidance on difference between entity-specific inputs used in VIU and market-participants inputs used in FVLCD.

(c) More guidance on how to calculate the discount rate. For example, the explanations provided in the Educational Material for IFRS 13 (2013) is a useful guidance. It is recommended updating and aligning the guidance in IAS 36 in this or other regard, e.g., the growth rate based on the Gordon growth model.

(d) Apply a simpler approach to deal with cash flows relating to leases as the current IFRS 16 standard requires the following adjustments to the cash flows in the VIU which are very complex and leads to divergence in practice:

   (i) Exclude the lease liability from the carrying amount of the CGU as it is treated as financing debt. Some say an entity does not include the liability in the CGU's carrying amount because that liability has a financing nature and paragraph 50(a) of IAS 36 states that estimates of future cash flows exclude the cash outflows from financing activities. In contrast, other say that the liability has an operating nature and accordingly, that it should reduce the CGU's carrying amount;

   (ii) Exclude payment of lease instalments from cash flow projections, but only for that part which leads to the recognition of a liability under IFRS 16;

   (iii) Assess the impact of contract renewals; and

   (iv) Adjust the discount rate to take into account this new "type of financing';

(e) The FVLCD of a publicly traded CGU is based on a quoted price, however in practice a control premium will be applicable to acquire a majority stake. Therefore, the current requirements in determining the FVLCD should be amended to include a control premium;

(f) Separate certain items currently included in goodwill, i.e., "technical" goodwill connected to deferred tax liability, as the "use" of this goodwill is directly related to the settlement of the related deferred tax liability and should not be shielded by other assets; and

(g) One user organisation suggests leaving goodwill on the balance sheet in perpetuity unless the business unit is subsequently closed or sold. This would help investors derive invested capital, might discourage management from over-paying for assets and would eliminate the debate about how to measure something that does not exist. This suggestion is not universally supported within the user organisation. Some members would prefer that goodwill is amortised as it does not last forever, and impairment testing tends to be over-optimistic. They regard amortisation over an appropriate period as a better alternative.

429 The professional organisation provides the following additional comments:

(a) Even though the removal of the restrictions on cash flows and post-tax input would result in a high convergence VIU and Fair Value Less Costs of Disposal (FVLCD) in practice, the "higher of" concept should be retained.

The VIU allows the inclusion of entity-specific synergies, better assess "for keeping" and is more easily documented. Furthermore, there may be differences between the two in cases where the fair value is observable (e.g., a listed subsidiary);

(b) The proposal in paragraph 4.55a of the IASB's DP to add more guidance on the difference between entity-specific inputs used in the VIU calculation and market-participant inputs used in the FVLCD is not supported. The current guidance is already comprehensive, and the issue relates more to practical application. One national standard setter agrees with this view if the IASB proceeds with the proposal to remove the restrictions in IAS 36;

(c) The alternative to require a company to select the method of management's intention of recovery is not supported. It may be difficult to operationalise relevant criteria in case the intent is to dispose of the asset(s) but the criteria in IFRS 5 Non-current assets held for sale and discontinued operations are not met; and

(d) The proposal in paragraph 4.55c of the IASB's DP to allow companies to test goodwill at the entity level or at the level of reportable segments is not supported as this would worsen the shielding problem. One national standard setter suggests that the IASB eliminates the requirement to allocate goodwill at the lowest level at which it is monitored for internal management purposes, such that goodwill should be allocated at the operating segment level before aggregation. In their experience the concept of “monitoring goodwill” is not well understood and often gives rise to discussion with preparers.

430 One considers that the IASB should consider adding further guidance on the allocation/ reallocation of goodwill to cash-generating units to improve the effective application of the impairment test. More guidance should also be provided for divestments.

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?

Proposals in the DP

431 The IASB has considered whether it should change the criteria for recognising intangible assets acquired in a business combination.

432 The IASB considered stakeholder feedback about whether to permit or require companies to include in goodwill identifiable intangible assets acquired in a business combination meeting a criterion such as the following (which partly overlap):

(a) *Specified types of intangible assets such as customer relationships, brands and non-compete agreements.*

(b) *Intangible assets not already recognised in the acquired company’s financial statements.*

(c) *Intangible assets that would not have been recognised in the acquirer's financial statements if generated internally.*

(d) *Intangible assets that do not meet the contractual legal criterion.*

(e) *Organically replaced intangible assets, as opposed to wasting assets.*

(f) *Intangible assets that have indefinite useful lives and are not already generating cash inflows largely independent of cash flows from other assets or groups of assets*

433 The IASB identified disadvantages of the approaches listed in the above paragraph:

(a) *Goodwill would be commingled with identifiable intangible assets with different characteristics, leading to a loss of information about those assets.*

(b) *Reducing the proportion of intangible assets recognised separately would not respond to the frequent calls to improve financial reporting by providing more information about intangible assets that are increasingly important in modern economies.*

(c) *If the IASB does not reintroduce amortisation of goodwill, then including intangible assets with finite useful lives within goodwill would lead to a loss of information about the consumption of those intangible assets. If the IASB reintroduces amortisation of goodwill, commingling these intangible assets with goodwill may make it even more difficult to determine an appropriate useful life for goodwill.*

(d) *Some additional complexity could arise. For example, if identifiable intangible assets are included within goodwill and subsequently sold, what profit should a company recognise on disposal?*

434 Furthermore, preparers have expressed varying views on the cost of implementing the current requirements. In addition, investors have mixed views on whether separate recognition of identifiable intangible assets provides useful information. Their views also vary on how to determine which intangible assets should be recognised separately to provide useful information.

435 Overall, the IASB concluded it did not have compelling evidence that it should permit or require some identifiable intangible assets to be included in goodwill. Thus, the IASB's preliminary view is that it should not make any changes.

EFRAG's tentative position

In considering the accounting for intangible assets, EFRAG thinks that it is necessary that the IASB takes into account the concerns of investors who want to compare companies that grow by acquisitions more easily with those that grow organically. EFRAG would therefore recommend that the issue on whether some intangible assets could be included in goodwill should be considered in a second phase of the project together with a revision of IAS 38.

Summary of constituents' comments

436 13 out of 22 respondents, represented by preparers, user organisation, professional organisation, regulator and national standard setters, support the proposal to not develop requirements to add intangible assets acquired in a business combination to the carrying amount of goodwill.

437 2 out of 21 respondents, support the proposal if the impairment-only approach is retained and otherwise support adding intangibles to the goodwill if amortisation is reintroduced. One respondent explains that their position depends on the accounting for internally generated intangible assets and therefore suggest a broader review of IAS 38. 5 out of 21 respondents do not agree with the proposal

and require adding certain intangibles to the carrying amount of goodwill. And finally, one respondent represents mixed views.

438 The respondents supporting the proposal use the following arguments:

(a) Considering recent changes on the prudential treatment of some intangible assets (software), proposals in another direction would create prejudice for the banking sector. The IFRS recognition criteria affect the prudential treatment, therefore any changes should be carefully assessed in order to avoid unintended consequences;

(b) Separate recognition provides useful information about the nature of the acquisition and helps better understanding the price paid for the acquisition;

(c) Combining intangible assets with goodwill obscures the nature of goodwill and deviates from the objective to improve the accounting and disclosures for goodwill. Furthermore, goodwill balances will be even more inflated, aggravating the problems that triggered the DP;

(d) Information on intangible assets, for example customer relationships and brands, might be useful for investors;

(e) The importance of intangibles in today's business models and the user's need for more information on intangible assets is increasing; and

(f) Separate recognition allows investors to better compare companies that grow by acquisitions and companies that grow organically.

439 Nonetheless, the respondents acknowledge challenges of separate recognition and that some intangible assets could be eligible to be included in the carrying amount of goodwill:

(a) By exception, some intangibles may not provide relevant information to users, for example trademarks;

(b) The difference in recognition criteria for internally generated intangible assets and intangible assets acquired in a business combination is conceptually inconsistent;

(c) Separate recognition might be complex and costly, however sufficient expertise is expected to be available. Some respondents confirm that recognition and measurement of intangible assets in the purchase price allocation can be complex and costly, but nowadays follow established rules commonly accepted by valuation experts and the accounting profession;

(d) The measurement of some intangibles, for example customer relationships and brands, are subjective and therefore questionable, except for fixed term wasting assets such as licenses. When measurement is perceived to be too subjective, some users ignore the intangible assets, therefore it is questionable whether the benefits outweigh the costs.

(e) Determining the amortisation period is also highly subjective. Customer lists have indefinite lives as they evolve over time to reflect the departure of old and the arrival of new customers. One can further argue that a prime aim of the marketing budget is to ensure that the customer list remains up to date. It is illogical to treat the customer list as a wasting asset as virtually every company will strive to ensure that the list evolves and remains valid. These types of acquired intangible are often referred to as ones which are "organically replaced through the P&L" such that the value does not erode over time. The income statement, if it is to be a measure of economic performance, should not show both the cost of maintaining the asset as well as the amortisation charge.

(f) Current disclosures are not satisfactory and associated amortisation is not economically useful;

(g) If amortisation is reintroduced, the assessment of whether the useful life of intangible assets identified in the PPA is finite or indefinite becomes more relevant and considering that identification and valuation of intangible assets like trademarks and brands are highly judgemental, rules need to ascertain that this assessment cannot be used for earnings management;

(h) A difference occurs in recognition when assets are acquired separately compared to assets acquired in a business combination;

(i) Few respondents questions why customer relationships without underlying contract can be recognised but assembled workforce cannot. The assembled workforce accounts for a growing part of goodwill that service-entities recognise over time and this economic trend cannot be ignored. Separate recognition of the workforce has the following advantages:

   (i) The amount of goodwill would be reduced arithmetically;

   (ii) The accounts would provide directly observable information to users;

   (iii) The elements accounted for could probably be amortised over useful lives which would be less arbitrary than that of goodwill; and

   (iv) The forthcoming developments on non-financial information will shed new light on these intangibles with, in the first instance, an objective of simple disclosure. It could be of use also for the IASB to consider the possibility of permitting the accounting recognition of certain items in the context of business combinations.

(j) The current valuation of identifiable intangible assets is already difficult and therefore not supported to recognise separately intangible assets currently included in the goodwill. This point can already be clarified without waiting for a review of IAS 38; and

(k) More guidance will be needed to effectively identify and separate intangible assets;

440 The professional organisation additionally comments that a robust purchase price allocation process and documentation automatically generates a lot more information than an entity is currently required to disclose. This includes information on acquired intangibles (e.g., the leading intangible asset, their useful life), how the internal rate of return compares to the cost of capital, which if disclosed may provide investors with more useful information on acquisitions. Nonetheless, we recognise that this information may be commercially sensitive. Therefore, if the IASB decides to pursue this idea, it is important to strike a balance between the usefulness of this information to investors and commercial sensitivity concerns of preparers.

441 One national standard setter agrees with the IASB's observation in paragraph 5.25(d) of its DP that not recognising separately intangibles that meet the identifiability criterion in IAS 38 would create complexities when an entity disposes of those assets.

442 Many respondents support to start a dedicated and comprehensive project to review the accounting for intangible assets. In particular, in the context of technological developments in the recent years. However, some respondents urge for narrow-scoped review on short term instead of waiting for a broader review on long term.

443 The respondents not supporting the proposal, and therefore supporting to add intangible assets to the carrying amount of goodwill use the following arguments:

(a) The standard obliges us to identify and value separately certain intangible assets whose evaluation is not always reliable. It might now be appropriate

to review these obligations, particularly in respect of those elements which are not amortisable. The approach proposed in paragraph 5.18 of the DP, which is an approach by default, might be a way to resolve this question, but does not address the question of new types of intangible assets which could be recognised separately;

(b) Intangibles are currently only used to lower the goodwill, because goodwill is perceived as evidence for overpayment. Additionally, amortising results in lowering the invested capital which has a positive impact on certain key ratios. This view is supported by a preparer organisation as separation is considered to be arbitrary to some extent and impacted by management preferences. The separation process could be amended to target clearly identifiable "core" intangibles;

(c) There are many intangible assets, that are recognised but still seen as goodwill by users. Only real intangible assets should be recognised, for example those that can be sold at an active market. Client relationships for example cannot be sold. The accounting for some intangibles acquired in a business combination, for example trademarks which are considered to have an indefinite useful live, should be reviewed;

(d) Intangible assets can be added to goodwill for pragmatical reasons. For example, the German Accounting Standards prohibit separate recognition if it cannot be measured reliably. However, this could result in risk that too many intangible assets will be included in goodwill increasing the shielding effect. Therefore, it is important to consider this;

(e) The derivation of a useful operating profit number is made more complicated. Many companies are moving to a version of EBITA to get around this. Analysts typically accept this as a better measure of profit as they see the non-wasting nature of many of these assets. When companies adopt a new reporting metric, it can be an indication that the standards are not working effectively.

(f) The information value will not decrease if intangible assets are included in the carrying amount of goodwill; and

(g) In practice, the difference between goodwill and certain intangibles (non-contractual customer relationships) is not clear as it is very subjective. It is questioned whether the benefits of separate recognition outweigh costs and whether it contributes to useful information. Should be further investigated and distinction between intangibles IFRS 3 and IAS 38 further clarified. Furthermore, should be considered if the exception in IFRS 3 for recognition is needed or should be the same as in IAS 38.

444 One preparer organisation commented on the list of criteria considered by the IASB to require companies to include intangible assets to the carrying amount of goodwill in paragraph 5.18 of its DP:

(a) Specified types of intangible assets such as customer relationships, brands and non-compete agreements - seems to us to be too "rules-based" without conceptual justification;

(b) *Intangible assets not already recognised in the acquired company's financial statements, intangible assets that would not have been recognised in the acquirer's financial statements if generated internally and intangible assets that do not meet the contractual-legal criterion* - would prevent the separate recognition of assets which are not recognised today and for which separate recognition would perhaps be justified; and

(c) *Intangible assets that have indefinite useful lives and are not already generating cash inflows largely independent of cash flows from other assets*

or groups of assets - could be complemented by the characteristic that there is an inherent difficulty in arriving at a reliable estimation of its value. The separate recognition of an intangible asset always provides useful information, even if it is not amortised, except when its value is not determinable in a reliable manner. This aspect annuls the benefit of separate recognition.

445 Two respondents agree with the current proposal if the impairment-only model is retained. If amortisation was reintroduced it could be reasonable and less costly to allow for some integration of the acquired intangible assets into the goodwill, considering their useful lives. One preparer organisation stated that separation of intangibles from goodwill can be limited to some clearly identifiable intangibles if amortisation of goodwill is reintroduced. Another respondent agrees with reduced importance of making distinction between intangible assets and goodwill when amortisation is introduced.

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?

Proposals in the DP

446 In July 2019 the FASB issued the Invitation to Comment: Identifiable Intangible Assets and Subsequent Accounting for Goodwill. The IASB's research project and the FASB's project are separate and although they exchange information, they are not working jointly on the projects. Nevertheless, they have been monitoring each other's work because the projects focus on similar topics because IFRS 3 and 'Topic 805 Business Combination' are largely converged.

447 In its Invitation to Comment, predominantly for public business entities, the FASB sought stakeholders' views about whether:

(a) *To change the subsequent accounting for goodwill. The FASB sought stakeholders' views on whether to reintroduce goodwill amortisation for public business entities or to further simplify the goodwill impairment test. Potential simplifications could include assessing goodwill for impairment following an event or change in circumstances that indicates goodwill is more likely than not impaired or providing an option to test goodwill at the company level.*

(b) *To modify the requirements for recognising intangible assets acquired in business acquisitions, the FASB sought stakeholders' views on whether to:*

   (i) *extend the private company option to public business entities*

   (ii) *establish a new principle-based criterion to determine which identifiable intangible assets should be included in goodwill; or*

   (iii) *include all intangible assets in goodwill.*

(c) *To add or change disclosures about goodwill and intangible assets. The Invitation to Comment discussed providing information on the key performance targets supporting an acquisition and information about performance against those targets for several years after the acquisition.*

However, the Invitation to Comment sought stakeholders' views on other ideas for new or enhanced disclosures because of concerns about:

(i) *the cost of providing such information;*

(ii) *the complexity of integration; and*

(iii) *the disclosure of forward-looking information.*

448 The FASB's Invitation to Comment therefore covered similar topics to the IASB's Discussion Paper. Some stakeholders have told the IASB that maintaining convergence between IFRS Standards and US GAAP is important to them.

449 Additionally, In March 2019 the Australian Accounting Standard Board published Research Report 9 Perspectives on IAS 36: A case for standard setting activity. This report considers IAS 36 impairment testing for all assets, not just for goodwill.

EFRAG's tentative position

EFRAG's responses to the questions in the DP do not depend on whether the outcome is consistent with US GAAP. However, EFRAG considers that the IASB outcome could be influenced by the FASB's current work.

Summary of constituents' comments

450 17 out of 18 respondents represented by preparers, professional organisation, user organisation, market organisation, regulator and national standard setters, support convergence with the FASB. One preparer organisation does not consider convergence to be important.

451 In general respondents prefer convergence but emphasise that it should not be the main goal.

452 Many respondents urge the IASB to reconsider carefully how the FASB has responded to the issues relating to the subsequent performance of acquisitions and urge the IASB not to introduce IFRS requirements which could disadvantage companies applying IFRS compared to companies applying USGAAP. One preparer organisation comments that its members have the impression that US companies disclose less information about acquisitions in the notes to the financial statements and more in MD&A/management commentary than users of IFRS and suggests that the IASB should look into this aspect of the issue.

453 Many respondents find convergence very important on the subsequent accounting for goodwill. One national standard setter finds convergence important because of level playing field reasons instead of aiming for uniform accounting standards as empirical evidence shows that the purchase price paid is impacted by subsequent accounting for goodwill. Another respondent explains that one of the most important arguments to implement the impairment-only model in 2004 was the level playing field argument: amortisation could lower financial results of IFRS preparers compared to USGAAP. Applying the same arguments, retaining the impairment-only while USGAAP requires amortisation would be beneficial.

454 Some of the national standard setters and the professional organisation, agree that convergence should be aimed for as it improves the comparability and transparency in the global markets.

455 One respondent does not consider convergence necessary. They acknowledge the competitive disadvantage when some important jurisdictions would still stay on the impairment only model while the IASB would reintroduce amortisation. Nevertheless, the IFRS accounting framework has meanwhile developed into a leading one. Therefore, introducing a change in the global leading standard for goodwill treatment would be a real 'game-changer'. Reporting entities which are not following the IFRS would face the expectations on the investors' side to provide

similar information on the potential amortisation charge as well to allow for comparability in investors' analysis.

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?

EFRAG's tentative position

EFRAG would consider that the DP could have included a discussion on separating goodwill into components. In addition, EFRAG suggest the IASB to develop more guidance on goodwill allocation to divested businesses and reorganisations. Finally, EFRAG is seeking views from its constituents on whether the IASB should consider introducing the reversal of goodwill impairment, including impairment losses recognised in an interim period.

Summary of constituents' comments

Preparers

456 One preparer indicated that the portion of goodwill resulting from the effects of deferred tax liabilities on acquisition is less than 5% of the recognised goodwill.

457 One preparer organisation noted the following:

(a) They disagreed with the view that management will be held (more) accountable when making a corporate operation by way of disclosures. This because of: (i) exaggerated influence given to disclosures in the financial statements when, at present, there are other mechanisms to verify the performance of a company and its top management (ii) shareholders, internal governing bodies, supervisors and regulators continually evaluate the level of competence of the management of an entity in aspects a lot wider than corporate acquisitions. Not taking this into account would diminish the importance of the current regulation and policies on corporate governance.

(b) They noted the DP should not give the impression that 'reasonable' is the price that generates less goodwill, with the risk of linking the payment of a non-reasonable price with benefits for the entity. As per the current prudential treatment, goodwill is deducted from CET1 capital, so it can no longer be understood that banks obtain a clear advantage derived from its recognition.

458 Another preparer organisation considered that the prohibition on the reversal of impairment of goodwill increases the pressure on the impairment test providing the example of the pandemic in the first half of 2020. In limited cases, for a restricted period following an impairment, reversals should be allowed when an entity can demonstrate the reason for the reversal is due to the evolution of assumptions used for estimation of the impairment. Examples would include WACC or the long-term growth rate. The respondent also referred to their response on the PIR for IFRS 10 relating to variations in percentage holdings, for example step acquisitions.

459 An insurer preparer organisation highlighted that the IASB would need to consider the impact on transition if goodwill amortisation is re-introduced and referred to the work of the German standard setter in this regard.

Users

460 A user organisation recommends separate disclosure of internally generated assets and those acquired during an acquisition with Atlas Copco as an example of good practice. The respondent argues that the information is available as it would not be possible to calculate the net asset total without. The disclosure would enable users

to obtain a better view of overall operating performance and the respondent notes that some acquired intangibles are operational in nature, e.g., fixed-term licences.

Auditors

461 One respondent suggests that the IASB field tests the proposals to understand whether the additional benefits to users would outweigh the costs for preparers. This would also help to assess to what extent the general objective of the DP would be met in practice.

462 Responses to EFRAG's questions to constituents: One respondent did not support changing the current accounting for goodwill relating to the deferred taxes mismatch. On reversals of the impairment of goodwill, they do not support the introduction of reversals of goodwill impairment. Firstly, they consider the conceptual reasons as set out in the Basis for Conclusions in IAS 36 *Impairment of Assets* still stand. If such reversals were allowed, they also consider that similarly to other assets, such reversals may not be widely used and so may be of limited value to address the problems with the impairment test.

Standard setters and regulators

463 One respondent considers that the issue around deferred tax liabilities and goodwill is best addressed by the reintroduction of the amortisation of goodwill. This would also render obsolete the question around the reversals of impairment which it considers to be the goal of a project like this.

464 Another respondent considers that the current prohibition of the reversal of goodwill impairment contributes to the reluctance to the recognition of a goodwill impairment. Furthermore, this treatment differs to that for indefinitely lived assets such as brands.

465 One respondent referred to their reply to question 11 about separating technical goodwill either as a separate intangible asset or component of goodwill that will be subject to amortisation or tested at the same level as the related deferred tax.

466 Another respondent observes that the IASB does not consider the possibility of separating goodwill into components. Whilst they concur that such a separation may imply complexities, they refer to the component of goodwill related to deferred taxes. Such a component of goodwill could be amortised during the same period in which the related deferred tax liabilities reverse in profit or loss. This portion of goodwill is due to an accounting mismatch from the measurement of deferred taxes under IAS 12 *Income Taxes*, rather than at fair value like the other assets and liabilities acquired in a business combination.

467 Another respondent recommends that the IASB provides further guidance where the business combination involve the acquisition of an entity with one, or only a few, assets with the tax base significantly lower than the related fair value(s). The respondent considers that it is not clear whether the resulting deferred tax liabilities should be included in the carrying amount of the CGU. If the goodwill and the deferred tax is allocated to the CGU a 'day one' goodwill impairment could occur under IAS 36.

Appendix 2 – List of respondents

CL001	ESBG	Europe	Preparer organisation
CL002	UniCredit		Preparer
CL003	Accountancy Europe (AE)	Europe	Professional Organisation
CL004	BNPP	France	Preparer
CL005	Insurance Europe-CFO Forum	Europe	Preparer organisation
CL006	ICAC	Spain	National Standard Setter
CL007	Comissão de Normalização Contabilistica (CNC)	Portugal	National Standard Setter
CL008	EFFAS	Germany	User organisation
CL009	DASC	Denmark	National Standard Setter
CL010	SFRB	Sweden	National Standard Setter

14 draft anonymous comment letters were received and included in this document.