Initial feedback received in response to EFRAG's M&A consultation.

Objective

1 The objective of this paper is to provide to TEG members with a summary of the initial feedback received from the M&A departments in response to the consultation launched by the EFRAG Secretariat on whether accounting for goodwill have an impact on M&A activities.

Background

2 IFRS 3 requires entities to recognise the goodwill as a residual difference between the purchase price paid to acquire a business and the fair value of net assets and liabilities acquired. This amount, if positive, is recognised in as an asset, is not amortised and is subject to yearly impairment test. The IASB is currently considering a possible change to the accounting for goodwill.

3 In order to assess whether the introduction of amortisation of goodwill would have any impact on M&A activities, including whether it could introduce an unlevel playing field for entities reporting under US GAAP and IFRS (in case of divergent accounting), the EFRAG Secretariat prepared and launched a very short questionnaire for M&A professionals.

Initial feedback received

4 The EFRAG Secretariat has launched the questionnaire to the EFRAG FIWG, EFRAG IAWG and big accounting firms. They have distributed the questionnaire to relevant persons within their internal M&A departments and their M&A advisory departments.

5 The EFRAG Secretariat has received eight answers in response to its consultation; including external advisor in relation to M&As (three), CFO (one), internal advisor of a decision maker of M&As (one) and decision maker of M&As (three).

6 The text below summarises the replies.

7 Five respondent agreed that how goodwill is accounted for in subsequent periods could impact the M&A activity (*they would expect the management of one entity to consider how it will account for the goodwill in subsequent periods when deciding on whether to acquire another entity*). Three respondents indicated that it could not affect.

8 Four respondents agreed that an approach under which goodwill is amortised over a short time period (in the example 5 years) in addition to being subject to a yearly impairment test will result in a decrease in the price an acquire is willing to be paying for a business. One respondent indicated that the current requirements (i.e. goodwill is only subject to a yearly impairment test - no amortisation) is the accounting

treatment under which the management of one entity would be less likely to acquire another entity or offer a higher purchase price. Another respondent noted that an approach under which goodwill is split into the different components the management assesses it to consist of (all the components of goodwill are subject to a yearly impairment test, the components that have a definite useful life are amortised over their useful life) is the accounting treatment under which the management of one entity would be less likely to acquire another entity or offer a higher purchase price. Two respondents did not address this question.

9 Five respondents agreed that the accounting requirements for how to account for goodwill subsequent to the initial recognition would generally affect a management's decision to acquire another entity or offer a higher price but not very much. Another respondent indicated that it would have a noticeable effect on the decision. Two respondents did not address this question.

10 Two respondents indicated that if goodwill should be amortised over 10 years in addition to being tested for impairment (instead of being accounted for under the current requirements) would result in slight decrease in the level of M&A activity. Four respondents indicated that it would not affect the level of M&A activity. Two respondents did not address this question.

11 Five respondents noted that if goodwill should be amortised over 10 years in addition to being tested for impairment (instead of being accounted for under the current requirements) it would result in a slight decrease in the price an entity will be willing to offer for another business. Three respondents indicated that it would not affect the price an entity would be willing to offer for another business.

12 Four respondents indicated that if goodwill should be amortised over 10 years and not be tested for impairment (instead of being accounted for under the current requirements) it would result in a slight decrease in the price an entity will be willing to offer for another business. Three respondents noted that it would not affect the price an entity would be willing to offer for another business. One respondent indicated that it would result in an entity being willing to offer a slightly higher price for another business.

13 Lastly, five respondents indicated that if goodwill should be amortised over 10 years in addition to being tested for impairment (instead of being accounted for under the current requirements) would not affect how the acquisition of a business is structured (e.g. in terms of use of variable consideration, type of consideration, method of achieving control (transfer of shares or repurchase of own shares). The other three respondents indicated that it would affect how the acquisition of a business is structured.