EFRAG Secretariat: Isabel Batista-Pirhonen, Galina Borisova, Laura Abeni, Didrik Thrane-Nielsen

Goodwill and Impairment

Identifiable intangible assets acquired in a business combination, total equity excluding goodwill, and other topics

Objective

1 This paper discusses the IASB tentative decisions taken in December 2022 on identifiable intangible assets acquired in a business combination, total equity excluding goodwill, and other topics.

Background

2 The IASB issued the Discussion paper *Business Combinations – Disclosures, Goodwill and Impairment* ('the DP') in March 2020 with a comment period that ended on 31 December 2020.

3 The DP included suggestions on improving the disclosures about business combinations by adding information about the strategic rationale and objectives for the acquisition including information about synergies as well as the metrics management plan to use to monitor achievement of those objectives; its subsequent performance; improving the accounting for goodwill by assessing whether the amortisation should be reintroduced and some other targeted improvements/simplifications to the current impairment test including the suggestion to only require a quantitative impairment test of cash-generating units ('CGUs') including goodwill to be performed when there would be an indication of an impairment.

4 EFRAG published its final comment letter in January 2021.

5 In September 2021 the IASB started a re-deliberation process on the preliminary views included in the DP. A summary of the IASB tentative decisions so far on the project is provided in the Appendix of agenda paper 08-01.

6 This paper focuses only on the tentative decisions taken in December 2022.

Identifiable intangible assets acquired in a business combination (AP18B)

IASB preliminary view

7 The IASB's preliminary view was that it should not change the recognition criteria for identifiable intangible assets that are acquired in a business combination (e.g., IFRS 3 *Business Combinations* requires an entity to recognise, separately from goodwill, all identifiable intangible assets acquired in a business combination).

Feedback on the IASB preliminary view

8 In summary, the feedback received on the DP was:

(a) most respondents, including many users, agreed with the preliminary view. In their view, goodwill and other intangible assets acquired in a business combination are different in nature and that recognising these assets separately provides better and more useful information;

(b) some respondents, including some users, disagreed with the preliminary view. In their view, separately recognising acquired intangible assets does not provide useful information and the costs of doing so outweigh the benefits.

9 In addition, some respondents suggested that the IASB undertake a broader scope project on intangible assets due to the increasing importance of intangible assets.

IASB Staff recommendations

10 The IASB Staff believed that the IASB should remain on its preliminary view.

11 In particular, the IASB Staff highlighted the following points:

(a) feedback received has shown that the IASB preliminary view is substantially shared;

(b) in November 2022, the IASB tentatively decided not to explore amortisation of goodwill further;

(c) changing the current recognition criteria would imply significant time and resources to explore the potential implications of including *some* intangible assets in goodwill with the concrete risk of delaying the project;

(d) in April 2022, the IASB decided to add to its research pipeline a project that will aim to comprehensively review the accounting requirements for intangible assets.

IASB decision

12 In line with the IASB Staff recommendation, in December 2022, the IASB tentatively decided to maintain its preliminary view and therefore to make no changes to the recognition criteria in IFRS 3 for identifiable intangible assets acquired in a business combination.

EFRAG comment letter

13 In its final comment letter, EFRAG suggested that the IASB should take into account the concerns of investors who want to compare companies that grow by acquisitions more easily with those that grow organically. Therefore, EFRAG 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.

Questions for EFRAG FR TEG

14 Does EFRAG FR TEG agree with the IASB tentative decision to maintain its preliminary view on recognition criteria for identifiable intangible assets acquired in a business combination?

Total equity excluding goodwill (AP18C)

IASB preliminary view

15 The IASB's preliminary view was to require an entity to present on its statement of financial position the amount of total equity excluding goodwill ('proposed presentation'). Entities would be required to present this amount as a free-standing item, and not as a subtotal within the structure of the statement of financial position.

16 The IASB believed that the proposed presentation would provide further transparency about the effect of goodwill and would give this amount more prominence[1].

Feedback on the IASB preliminary view

17 Almost all feedback received expressed disagreement with the presentation proposed by the IASB in the DP. In particular, respondents highlighted the following main points:

(a) the proposed presentation was unnecessary because users could easily compute total equity excluding goodwill based on information already in financial statements (e.g., goodwill balance on the statement of financial position is presented separately from intangible assets);

(b) the proposed presentation lacked conceptual basis not being in line with the requirements included in the *Conceptual Framework for Financial Reporting*;

(c) the proposed presentation could cast doubt on whether goodwill is an asset and on the reliability of the impairment test.

18 Respondents also believed that the IASB should focus on addressing the subsequent measurement of goodwill, and not use presentation as a substitute.

IASB Staff recommendations

19 The IASB Staff made the following considerations:

(a) in February 2022, as part of its deliberations on its project on *Primary Financial Statements*, the IASB tentatively decided to require entities to present goodwill as a separate line item on the statement of financial position. This information is sufficient to highlight the effect of, and give sufficient prominence to, goodwill; and

(b) feedback received does not indicate that the proposed presentation would be useful (on the contrary, many users believed that the proposed presentation would be misleading).

20 For these reasons, the IASB Staff recommended not proceeding with the preliminary view to require an entity to present on its statement of financial position the amount of total equity excluding goodwill.

21 In addition, the IASB Staff believed that disclosing the total amount of equity excluding goodwill in the notes would not give as much prominence to this amount as presenting on an entity's statement of financial position. Accordingly, the IASB Staff believed that this option should not be further considered by the IASB.

IASB decision

22 In line with the IASB Staff recommendation, in December 2022, the IASB tentatively decided against proceeding with its preliminary view and therefore tentatively decided not to require an entity to present the amount of total equity excluding goodwill as a separate line item on its statement of financial position.

EFRAG comment letter

23 In its final comment letter, EFRAG did not support the IASB proposal to require entities to present on their statement of financial position the amount of total equity excluding goodwill.

[1] Paragraphs 3.107–3.115 of the DP.

Questions for EFRAG FR TEG
24 Does EFRAG FR TEG agree with the IASB tentative decision not to require an entity to present the amount of total equity excluding goodwill as a separate line item on its statement of financial position?

Other topics (AP18D)

IASB Staff recommendations

25 The IASB Staff analysed the suggestions from respondents to the DP[2] for additional topics to be considered in the *Goodwill and Impairment* project.

26 The IASB Staff recommended the IASB includes only the following two additional topics suggested in the project:

(a) requiring an entity to disclose goodwill by reportable segment; and

(b) how the requirements in IAS 21 *The Effects of Changes in Foreign Exchange Rates* relating to the level at which goodwill balances are translated interacts with the level at which goodwill is tested for impairment applying IAS 36 Impairment of Assets.

27 The IASB Staff suggested that the IASB considers these two issues in deliberating possible improvements to the effectiveness of the impairment test of CGUs containing goodwill.

28 The table below lists the suggested topics that the IASB Staff **recommended not to include in the project**, with an indication of the position expressed by EFRAG in its final comment letter.

Feedback received	IASB Staff's analysis	EFRAG's position
Initial measurement of non-controlling interests		
• It is unclear whether paragraph 19 of IFRS 3 was intended to limit the application of the 'proportionate share of net assets' approach in measuring non-controlling interests or was intended as a requirement on how that approach should be applied. • The financial results of entities initially measuring non-controlling interests using the 'proportionate share of net assets' approach are not comparable with the financial results of entities using the fair value approach. • Goodwill attributable to non-controlling interests is not an asset of the reporting entity, and entities should therefore not be allowed to recognise such an asset when measuring non-controlling interests applying the fair value approach.	• In developing IFRS 3, the IASB was aware that permitting a measurement choice would result in differences between entities using the different measurement options (IFRS 3, BC217 – BC218). • In the context of the PIR of IFRS 3, the IASB concluded that the measurement of non-controlling interest was a low priority area. • In both the 2015 Agenda Consultation and the Third Agenda Consultation the IASB did not identify the measurement of non-controlling interests as a priority area.	EFRAG did not identify any issues on this topic.

[2] The summary of the feedback received is reported in the AP18E of the May 2021 IASB meeting.

<table>
<tr><td colspan="3">Accounting for non-controlling interests after a business combination</td></tr>
<tr><td>There is a lack of guidance on how to account for equity transactions with non-controlling interests that do not result in a loss of control, especially when the non-controlling interest was initially measured using the ‘proportionate share of net assets’ approach. Those transactions may overstate goodwill or could result in greater headroom that ‘shields’ goodwill from impairment losses.
It is unclear how entities should account for settlement of pre-existing relationships with non-controlling interests if those entities have initially measured the non-controlling interests using the ‘proportionate share of net assets’ approach.
An entity’s goodwill balance should be adjusted for subsequent changes in the ownership interests in a subsidiary that do not result in loss of control.
It is unclear how to allocate impairment losses between non-controlling interests and owners of the parent entity if the CGU giving rise to the impairment loss includes both subsidiaries with non-controlling interests and subsidiaries without non-controlling interests.</td><td>In the context of the PIR of IFRS 10 Consolidated Financial Statements, IFRS 11 Joint Arrangements and IFRS 12 Disclosure of Interests in Other Entities, the IASB concluded that these issues were a low priority area.
In the Third Agenda Consultation the IASB did not identify these issues as a priority area.</td><td>EFRAG did not identify any issues on this topic.</td></tr>
<tr><td colspan="3">Recognising assets acquired and liabilities assumed in a business combination at their acquisition-date fair values</td></tr>
<tr><td>Fair value adjustments made to assets acquired and liabilities assumed in a business combination affect the financial performance of the reporting entity in future periods (e.g., inventory adjustment). The financial impact caused by fair value adjustments on acquisition distorts the operating margin reported by the entity post-acquisition.
It was highlighted a conflict between the measurement principles in IFRS 3 (based on fair value) and in IFRS 15 Revenue from Contracts with Customers (based on the transaction price) that in its view should be addressed.</td><td>In the context of the PIR of IFRS 3, the IASB acknowledged the difficulties, but concluded that fair value remains the best approach for measuring the assets acquired and the liabilities assumed in a business combination.
The comments raised by respondents to the DP do not highlight new information.</td><td>EFRAG did not identify any issues on this topic.</td></tr>
<tr><td colspan="3">Specific components of goodwill</td></tr>
<tr><td>The IASB should reconsider requiring entities to separate goodwill into components and</td><td>When developing the DP, the IASB rejected the approach of separating goodwill into components and</td><td>EFRAG would consider that the DP could have included a discussion on separating goodwill into components although EFRAG noted the concerns</td></tr>
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<td>accounting for the different components separately.
• It was suggested exploring how to better account for 'technical goodwill' that results from deferred tax liabilities arising from fair value adjustments made to assets acquired and liabilities assumed in a business combination. In particular, it was suggested requiring entities to derecognise such goodwill when the corresponding deferred tax liabilities are derecognised.
• If the IASB decides not to do so, the IASB should clarify that a component of goodwill that resulted from the recognition of a deferred tax liability should be tested for impairment at the level at which the deferred tax liability is recognised.</td>
<td>accounting for the components separately because:
• it would increase the complexity and subjectivity of the subsequent accounting for goodwill; and
• goodwill cannot be measured directly and, therefore, it is doubtful the different components of goodwill could be measured reliably.
No convincing arguments have been provided to change the IASB's views in the DP.</td>
<td>around reliability of allocating amounts to such components.</td>
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<tr>
<td colspan="3">Acquisition of assets</td>
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<td>• There is misalignment between the accounting for business combinations and the accounting for the acquisition of assets that are similar in nature to business combinations.</td>
<td>• When developing the revised IFRS 3, the IASB considered whether to expand the scope of IFRS 3 to all acquisition of groups of assets and decided not to do so because doing so would require further research and deliberation of additional issues and could delay the implementation of the revised IFRS 3's improvements.
• As results of feedback received during the PIR of IFRS 3, the IASB decided to add a project to clarify the definition of a business (the amendment to IFRS 3 was issued in October 2018).
• No convincing arguments have been provided to change the IASB's view.</td>
<td>EFRAG did not identify any issues on this topic.</td>
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<tr>
<td colspan="3">Measurement of the consideration transferred</td>
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<td>• If the consideration for the business combination includes equity financial instruments, there is often a difference between the goodwill measured on acquisition date and the goodwill if it were measured at the date of the acquisition agreement due to changes in fair value of those instruments between those dates.
• The amount of goodwill recognised in financial statements is misstated because it does not represent the amount management intended to pay to acquire the business and therefore does not help to hold management to account for their acquisition decisions. It was suggested</td>
<td>• Paragraph BC338–BC342 of IFRS 3 discussed the reason the IASB decided that the fair value of equity securities issued as consideration in a business combination should be measured at the acquisition date.
• No convincing new arguments have been provided to change the IASB's views.</td>
<td>EFRAG did not identify any issues on this topic.</td>
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requiring entities to disclose this difference.		
Definition of goodwill		
It was suggested reviewing the definition of goodwill and clarifying that goodwill includes both the value of going concern as well as expected synergies	• This comment would have been relevant in considering any changes to the accounting for goodwill. • In November 2022, the IASB decided not to consider further the subsequent accounting for goodwill.	EFRAG did not identify any issues on this topic.
IAS 1 Presentation of Financial Statements		
The IASB should prevent entities from being able to window dress their financial results by prohibiting entities from classifying impairment losses recognised on goodwill as an unusual expense as proposed by the IASB's *Primary Financial Statements* project	In September 2022 the IASB tentatively decided to not proceed with specific requirements for unusual income and expenses as part of IASB's *Primary Financial Statements* project.	EFRAG did not identify any issues on this topic.
IAS 28 Investments in Associates and Joint Ventures		
The IASB should consider whether, and if so how, its preliminary views would apply to investments accounted for using the equity method.	The project is focused on business combination and consider other types of investment would be beyond the scope of this project.	EFRAG did not identify any issues on this topic.
IAS 36 Impairment of Assets		
Difficulties were highlighted in determining cash outflows when applying IAS 36 to CGUs containing right-of-use assets recognised applying IFRS 16 Leases. In particular: • The definition of a CGU in paragraph 6 of IAS 36 does not include liabilities, and paragraph 50(a) of IAS 36 states that estimates of future cash flows should not include cash inflows or outflows from financing activities. • Preparers find it difficult to adjust management budgets to separate cash flows relating to leases that are included in the lease liability applying IFRS 16 from cash flows relating to leases that are not included in the lease liability. • It was suggested allowing entities to include lease liabilities relating to right-of-use assets in the carrying value of a CGU and cash flows related to financing liabilities when estimating value in use. • Paragraph 33 of IAS 36 states that when an entity estimates value in use, cash flow projections and forecasts based on budgets shall cover a maximum period of five years,	• This project is not intended as a review of IAS 36. • The matter raised relates to the interaction of IFRS 16 and IAS 36. • Consequently, the matter raised goes beyond the scope of the project.	EFRAG has been informed that there is divergence in practice regarding how leases are incorporated in the value in use calculation. Namely: • how to take into account reinvestments in leased assets when the period for the cash flow projections exceed the lease term; • the possibility to include lease liabilities (and the cash outflows) in a CGU when calculating value in use. Preparers find it costly to separate the cash flows related to the liability from other cash flows related to the lease when the lease liability is not included in the calculation of the value in use of a CGU. Therefore, EFRAG suggested that the IASB should simplify the impairment test by stating that when calculating value in use, the lease liabilities and the related cash outflows could be included in the calculation of the value in use. EFRAG notes that such an amendment may raise questions around the treatment of other financing activities that are similar in nature to leases and so a broader topic may need to be considered in addressing this issue.

unless a longer period can be justified. • It was suggested providing guidance for cash flows relating to right-of-use assets beyond the forecast period, including guidance for cash flows from reinvesting these assets at the end of the lease term.		
The IASB should require entities to incorporate Environmental, Social, and Corporate Governance (ESG) considerations when forecasting future cash flows for impairment tests.		EFRAG did not identify any issues on this topic.

IASB decision

29 The IASB tentatively decided in line with the IASB Staff recommendations.

30 During the meeting discussion, **it was highlighted that the interaction of IFRS 16 with the impairment test is proving to be a developing issue in Europe**, and that it may therefore be worth considering the respondents' feedback on this issue in the project's scope.

Questions for EFRAG FR TEG

31 Does EFRAG FR TEG agree with the IASB tentative decision to include in the project the two topics mentioned in paragraph 26?

32 Does EFRAG FR TEG agree with the IASB tentative decision not to include in the project the topics listed in the table in paragraph 28?

33 Does EFRAG FR TEG believe that the IASB should consider other issues in the project? Please, explain.