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35 Square de Meeûs
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Belgium

**Discussion Paper “Goodwill Impairment Test: can it be improved?”
Comments by the French Society of Financial Analysts (SFAF)
Financial Analysis and Accounting Commission**

Dear Sir,

The French Society of Financial Analysts, SFAF (Société Française des Analystes Financiers), is very pleased to submit its contribution as part of the consultation undertaken by the EFRAG on the Discussion Paper “*Goodwill Impairment Test: can it be improved?*”.

SFAF represents more than 1,500 members in France and is itself a member of the European Federation of Financial Analysts Societies (EFFAS) which comprises 26 member organizations representing more than 15,000 investment professionals. Its Accounting and Financial Analysis Commission intends to represent analysts and fund managers in the debate on accounting standards. Financial analysts are among the principal users of corporate financial statements and therefore wish to express their opinion on the implementation of new or revised accounting standards.

As an introductory statement, as users of financial information, we strongly agree with the general statement that current standard (IFRS 3) relies on an impairment test that, in real life, delivers only “too late, too little” impairment being accounted for. For wider comments on the standard, see our comments at the end of this letter (and the references included).

Q1.1 Do you agree with the additional guidance on how an entity should allocate goodwill?

We believe that some companies may be tempted to allocate goodwill to CGU where impairment is less probable (i.e. CGU with “headroom goodwill”). We have also in mind some re-allocation of acquired goodwill to other CGUs in a second stage, with absolutely no impairments for years after while it is obvious that an impairment should have been made. We thus believe that having additional guidance on goodwill allocation (and subsequent re-allocation) would be a plus.

The examples provided in the document should be clearer, with limited options / choices. There is no explanation on what basis the goodwill amounts allocated to each CGU has been determined nor calculated. As noted in the discussion paper, there are some standard-setting work on “headroom goodwill” under way. It would thus be necessary to solve this problem first.

Q1.2 Do you have any other suggestions to improve this area of the goodwill impairment test?

See above.

Q2.1 Do you agree with the introduction of an initial qualitative assessment?

We do not support an approach where the impairment test could be postponed, based on an initial judgment. The (flawed) annual impairment test is the counterpart (see Q3.4) of the no amortization concept: it cannot be removed. As stated the “too little, too late” syndrome has proved that the standard is, already, not working properly: removing the annual obligation would only increase the syndrome.

Nevertheless, it does not preclude a company to do such an exercise, to better understand the factors having an impact on the value of the goodwill.

Q2.2 Do you have any other suggestions to improve this area of the goodwill impairment test?

No, specifically.

Q3.1 Do you agree with having a single method for determining the recoverable amount?

We think that combining *fair value* with *value in use* have added complexity, especially as both approaches are not based at all on the same assumptions. In principle, we would argue that the application of one method will be more reasonable, comparable and understandable. But each of the two methods has its own drawbacks.

As a conclusion, it seems difficult to choose one of the two methods as a single one to be used on a compulsory manner. Choosing one method simply reflects how a company estimates the value of its acquisition. We thus suggest that the company should explain the rationale behind the choice of the method used for determining the recoverable amount and keep this method along the years.

Q3.2 Do you agree with the inclusion of future restructurings in the calculation of the value in use?

For users the disclosure of relevant information is always advisable. In this case the inclusion of restructuring information would be relevant to the extent that the future restructuring will materialize as expected and within a reasonable period of time. We suggest that a group could not include restructuring beyond a three years period. Presenting potential benefits from restructurings in the calculation of the value in use should be done on the basis of a solid plan for implementation. And the reporting entity should disclose that this impairment test is based on assuming some restructuring.

Q3.3 Do you agree with allowing the use of a post-tax discount rate?

Entities and users customarily use a free-market discount rate to calculate WACC and DCF (even though we believe this valuation method can be used to justify whatever the management wants). We will agree with using a post-tax rate for calculation purposes as the relevance of the results will not be affected while being more consistent as the basis for calculation by entities and users.

An entity using pre-tax discount rates should however explain the reason for that and disclose the basis for calculation.

Q3.4 Do you agree that the impairment test should target internally generated goodwill? Is the goodwill accretion and acceptable way to do so?

One of the fundamental flaws of the current approach is that the impairment test compares the recorded goodwill (due to an acquisition) with the goodwill existing for the CGU at the time of the test. This latter includes goodwill generated internally after the business combination, which under current rules, is not considered as an asset. This was clearly recognised by the IASB Board when IFRS 3 was drafted (see BC 131E: *The Board acknowledged that if goodwill is an asset, in some sense it must be true that goodwill acquired in a business combination is being consumed and replaced by internally generated goodwill*).

The impairment test is really the cornerstone of the current approach (see BC 131G: *The Board agrees that IF a rigorous and operational impairment test could be devised...*). We believe that this aggregation of acquired and internally generated goodwill is one the main reasons of the current, and widely recognised, practice of “too little, too late” impairments.

Tracking the internally generated goodwill is thus a good idea. Unfortunately, as goodwill is defined as the part of the valuation that cannot be explained by assets and liabilities, a kind of residual, acquired goodwill and internally generated goodwill are mixed together and it is quite difficult to separate the two components. We thus have serious doubts that it could be possible to track the internally generated goodwill in an objective and operational manner.

In spite of that very significant difficulty, the goodwill accretion method could be a reasonable compromise to manage the current problem. We would suggest that the discount rate is fixed at the beginning of the business combination, so as to avoid having too many moving parts in the complete test, so that it could deliver whatever the accountant wants.

Finally we note that the choice of discount rate is, in fact, choosing an amortization period for the internally generated goodwill. This is inconsistent with the (wrong) current standard which states that *[the Board] observed that the useful life of acquired goodwill and the pattern in which it diminishes generally are not possible to predict* (BC 131E).

Q3.5 Do you have any other suggestions to improve this area of the goodwill impairment test.

Our views to improve this area are stated in the previous comments.

Beyond the subject of the impairment test, we would like to take the opportunity to remind EFRAG that SFAF has repeatedly said the IFRS 3 standard was flawed (as soon as ED 3 was published, we stressed that it could not work properly¹).

When the IASB launched its Agenda Consultation, in 2015, business combination was identified by SFAF² as one of the top three subjects that the IASB should tackle quickly, as demonstrated by the widely recognized “too little, too late” syndrome. In particular, we stressed that the syllogism that goodwill is an undefined useful life can imply NO amortization, is flawed: all other assets (including very tangible ones) have an expected useful life that is difficult to estimate. As stated above, we note that the test is comparing acquired goodwill with the sum of acquired goodwill, pre-existing goodwill and internally generated goodwill: the test is thus, by no means, able to guarantee that the acquired goodwill will be impaired when needed. The simple fact the standard-setters are discussing “headroom goodwill” and “internally generated goodwill” is a proof of this fundamental flaw.

Finally, we recently stressed in the FRC consultation on cash-flows statements that the link between the income statement and the cash-flows statement is of central importance for users. Having no amortization of goodwill while having cash paid for it, is just cutting this very important link.

We are still disappointed by the IFRS 3 post-implementation review, with almost no result as of today. The fact that US GAAP have simplified the impairment test is not an acceptable

¹ See our 2003 comment letter, available at www.sfaf.com/download/29/

² See our complete letter, available at www.sfaf.com/download/157/

argument: simplifying a test that is already not delivering the effect it pretends to deliver is simply not the right direction. Finally, as the current IFRS 3 was implemented mostly to converge with US GAAP (at a time where FASB was forced not to implement systematic goodwill amortization), as stated at this time, as users, we strongly favor good (workable and working) standards over (bad) converged standards.

We thank you for the opportunity given to us to provide our view on such important aspects of financial reporting for users. If you would like to further discuss the views expressed in this letter please do not hesitate to contact us.

Yours faithfully,



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