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FEEDBACK STATEMENT

DISCUSSION PAPER ON GOODWILL IMPAIRMENT TEST

xx March 2018



Introduction

In June 2017, EFRAG issued the Discussion Paper [Goodwill Impairment Test: Can it be improved?](#) ('DP'). Comments were requested by 31 December 2017.

EFRAG is now issuing a feedback statement which describes the main comments received.

Why was this Discussion Paper written?

When responding to the Short Discussion Series Paper, [Should Goodwill still not be amortised?](#), published in 2014 together with the ASBJ and the OIC, many constituents considered that impairment was a challenge in practice and that there was room to improve the guidance in IAS 36 *Impairment of Assets*.

After considering the feedback received and EFRAG's quantitative study on goodwill, [What do we really know about goodwill impairment?](#), the EFRAG Board agreed that work should be continued on potential improvements to the impairment model in IAS 36.

The objective of the DP published in June 2017 was to expose potential amendments to the impairment test and gather constituents' views.

EFRAG considered that the objectives of the amendments should be to:

- a) enhance the application and effectiveness of the impairment test, which should mitigate concerns that recognition of impairment losses may not be timely; and
- b) reduce complexity and achieve a better balance between costs and benefits.

Responses from constituents

Twenty-two comment letters were received in response to the DP. A list of respondents is in the Appendix to this feedback statement. All [comment letters received](#) are available on the website of the European Financial Reporting Advisory Group (EFRAG).

Purpose and use of this feedback statement

This feedback statement has been prepared as a formal record of the responses received. It summarises the messages received from constituents and notes any key themes identified.

The IASB is currently considering whether to change the existing requirements of IFRS 3 *Business Combinations* and IAS 36 *Impairment of Assets* to improve the way these Standards are applied. The feedback received on the DP will be used by EFRAG in developing its response to any future IASB proposals arising from its Goodwill and Impairment research project.

This feedback statement should be read in conjunction with the [DP](#), which is available on the EFRAG website.

Summary of the responses received

Overview of the feedback received

In general, respondents appreciated EFRAG's efforts to stimulate the debate on potential improvements to the goodwill impairment test. In particular, some respondents welcomed EFRAG's initiative to engage with European constituents during the early phases of the IASB's research work.

Nonetheless, some expressed concerns about the fact that some of EFRAG's suggestions could increase complexity/costs and asked for future improvements to be mainly focused on simplifying the goodwill impairment test and reducing costs for both preparers and users. In addition, some respondents noted that the DP did neither address the broader issue of whether goodwill amortisation should be reintroduced nor the existing issues on other intangibles.

When referring to EFRAG's suggestions, respondents generally agreed with the inclusion of future restructurings in the calculation of the value in use ('VIU') and allowing the use of a post-tax discount rate as both suggestions would reduce complexity and application costs of current requirements. There was also some support for the introduction of a qualitative assessment of the likelihood of an impairment. Nonetheless respondents expressed concern that this could affect the timeliness of goodwill impairments. Finally, there was less support for the remaining suggestions included in the DP as respondents considered that they would, to some extent, increase complexity and costs without clearly enhancing the effectiveness of the impairment test.

How to allocate goodwill to cash-generating units ('CGUs')

In the DP EFRAG suggested additional guidance on the allocation of goodwill to CGUs and disclosures on the break-down of goodwill by cash-generating unit ('CGU') to address some of the issues that arise in practice. When replying to Question 1 of the DP, respondents provided mixed views. Some would welcome additional guidance as it would bring more direction and discipline to preparers on how to allocate goodwill. However, others considered that IAS 36 already allowed entities to use its judgment to determine an appropriate method to allocate goodwill to the CGUs and that EFRAG's proposals seem to be a rule-based and driven by anti-abuse concerns. Still, some suggested that the allocation methods proposed in the DP could become part of the illustrative and non-mandatory guidance accompanying IAS 36. Finally, many respondents did not support additional disclosures as it would be difficult and onerous to track and assess each individual component of goodwill over time.

Qualitative assessment ('Step Zero')

In the DP EFRAG discussed the introduction of a 'Step Zero' in the impairment test to reduce application costs when the likelihood of an impairment is remote. The majority of the respondents generally welcomed the introduction of the Step Zero as the requirements in IAS 36 for the calculation of the recoverable amount are complex, costly and have to be performed at least annually even if there is no indication of an impairment and the CGU has a significant headroom. Some respondents also noted that the exception in paragraph 99 of IAS 36 was rarely used and was subject to strict conditions. Those that disagreed with the Step Zero were mainly concerned that it would not significantly reduce the operational costs while likely delaying the recognition of goodwill impairments.

Single calculation approach

In the DP EFRAG discusses the possibility of having a single calculation approach to calculate the recoverable amount as a way to simplify the impairment test. The majority of the respondents that replied to this question did not support the introduction of a single method for determining the recoverable amount as it would not result in a significant simplification (entities are not currently required to calculate both VIU and *fair value less cost of disposal* ('FVLCD')) and that both VIU and FVLCD were considered relevant for the calculation of the recoverable amount. Nonetheless, many respondents considered that the VIU was the most appropriate method to calculate the recoverable amount and considered that the VIU should be retained if a single method was to be introduced.

VIU and future restructurings

In the DP EFRAG discusses the possibility of allowing consideration of cash flows from future restructurings to increase the relevance of the VIU calculation. Most of the respondents supported EFRAG's suggestion as it would take into consideration management's views of the business and simplify the impairment test (it would allow entities to use directly their budgets and forecasts, which are likely to include the impact of future restructurings without making artificial adjustments to remove them). Nonetheless, a number of respondents called for some level of assurance. For example, future restructurings would have to be approved by management and this should be a requirement.

VIU and discount rates

In the DP EFRAG discusses the possibility of allowing the use of a post-tax rate to simplify the calculation of the VIU and reduce the cost when entities only have observable post-tax discount rates for an asset/CGU. Almost all respondents supported allowing the use of a post-tax rate since entities often conduct the impairment tests on a post-tax basis with an additional iteration simply to derive a pre-tax discount rate. Therefore, the introduction of a choice would simplify the calculation of the VIU and reduce costs.

Targeting internally generating goodwill

In the DP EFRAG discusses the introduction of a goodwill accretion approach in order to eliminate the effect of the internally generated goodwill. In general, respondents acknowledged that the basic assumption underlying the goodwill accretion approach and its objective. However, the majority of the respondents did not support EFRAG's goodwill accretion approach as it would add complexity and subjectivity to the goodwill impairment model. In addition, respondents argued that if acquired goodwill is an asset that is being consumed and decreasing over time, then the discussion should be focused on the reintroduction of goodwill amortisation, which is a simpler approach.

Nonetheless, two users' representative associations considered that the goodwill accretion approach could be a reasonable compromise to solve the issues related to internally generated goodwill and timeliness of impairments.

References to EFRAG DP and EFRAG presentation

After the publication of the DP in June 2017, EFRAG's proposals and questions were mentioned in a number of accounting journals, IASB Agenda Papers and on a number of websites. In addition, it was discussed in the context of a number of different events and meetings.

References to the DP on the internet:

- Newsletters and updates from auditing firms, professional organisations and national standard setters;
- Professional organisations and national standard setters announcing their responses to the consultation on their website;
- Professional organisations that discussed the DP in their meetings;
- References in accounting journals such as *Accountant (NL)*, *Betriebs-Berater (DE)*, *Der Betrieb (DE)*, *KoR (DE)*, *La Revue Fiduciaire (FR)*, *World Accounting Report*; and
- IASB Agenda Papers.

Outreach events and meetings

EFRAG presented its DP at the joint outreach event in Milan in September 2017 (see the [feedback report](#) on our webpage). Some of the key messages received include:

- users need entity-specific information about a CGU and a clearer link between the CGUs and the lines of business in the segment report;
- participants welcomed EFRAG's effort to promote the debate around the goodwill impairment test but questioned the goodwill accretion approach from a conceptual and cost-benefit perspective, and
- instead of focusing on simplification of the impairment test, the IASB could consider providing "anchors" to preparers to reduce the subjectivity of the impairment test (e.g. more use of market inputs);

EFRAG presented its DP at the Accounting Standards Advisory Forum (ASAF) in September 2017 (see [IASB summary of the meeting](#)). At the meeting ASAF members:

- welcomed EFRAG DP and its effort to address the shield effect derived from the internally generated goodwill. One member detailed that the goodwill accretion approach had the benefit of identifying impairment losses sooner. One other noted that the accretion approach aimed to remove a shielding effect and that this effect could arise for other assets, such as other indefinite-lived intangible assets;
- expressed concerns that the goodwill accretion would add complexity to the current impairment testing model and raised specific concerns. For example, members:
 - highlighted that the amount of goodwill accretion was not calculated on a compound basis, making it inconsistent with its underlying assumption;
 - noted that the goodwill accretion approach would not identify an impairment loss unless the estimated future growth rate was less than the growth rate assumed at the date of the acquisition;
 - considered that it would further increase the subjectivity of the goodwill impairment model and would conflict with standards setters' efforts to reduce the complexity of the standards;

- were concerned about how to measure the impact on a decrease of the original goodwill in the CGU;
- considered that it would be difficult for preparers to understand the new approach;
- argued that requiring additional disclosure would be a better solution than making the impairment test more complex.
- provided different views on the use of a single method for the calculation of the recoverable amount. For example, some members:
 - noted that if a single method was introduced for all the assets within the scope of IAS 36 Impairment of Assets, that would be a significant change;
 - thought the recoverable amount should be calculated based on the FVLCD. This would remove the arbitrary distinctions on the effect future enhancements and restructuring;
 - commented that the VIU could differ significantly from the FVLCD in some industries. Thus, if the VIU would become the sole basis for determining recoverable amount, there could be significant impairment losses in some industries (e.g. mining industry);
 - supported using the FVLCD or VIU depending on how an entity expects to recover the assets, in the light of its business model;
 - considered that the allocation of goodwill should be simplified and the impairment methodology needed to address deferred tax issues.
- mentioned that goodwill was not the present value of excess future returns but a residual amount, and thus it should be amortised over some specific period.

EFRAG also presented the DP paper to the Accountancy Europe (AE), European Federation of Financial Analysts Societies (EFFAS) and the Corporate Reporting Users' Forum (CRUF). Their comment letters are analysed below.



Analysis of responses

In general, respondents welcomed the DP and appreciated EFRAG's efforts to stimulate the debate on potential improvements to the goodwill impairment test and related disclosures. In particular, some respondents welcomed:

- EFRAG's aim to influence future standard-setting developments by engaging with European constituents and providing timely and effective input to early phases of the IASB's related work; and
- the objectives of the DP and its focus on improvements to the impairment test.

Nonetheless, a few respondents considered that future improvements to the impairment test of goodwill should be focused on simplifying the goodwill impairment test and reducing costs for both preparers and users. Similarly, some respondents expressed concerns about the fact that some of EFRAG's proposals could lead to increased complexity (e.g. additional guidance on the allocation of goodwill) and invited EFRAG to focus on "quick wins" (i.e. simplification of the IFRS requirements).

In addition, a number of respondents noted that the DP did neither address the broader issue of whether goodwill amortisation should be reintroduced nor the existing issues on other intangibles. Some of these respondents provided different views on how the IASB's research project should proceed. For example, these respondents called for:

- the reintroduction of goodwill amortisation;
- further initiatives that explore the reintroduction of goodwill amortisation, which would further align IFRS Standards with IFRS for SMEs and the European Accounting Directive; and
- introduction of an accounting policy choice for the accounting for goodwill (between amortisation and impairment-only approach) at the reporting entity level with appropriate disclosures.

Finally, one respondent supported the creation of an EFRAG Goodwill Accounting Working Group.

Question 1 - How an entity should allocate goodwill

In paragraphs 2.3 to 2.22 of Chapter 2 EFRAG discusses additional guidance on the allocation of goodwill to a CGU and disclosures on the break-down of goodwill by CGU.

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

Additional guidance on allocation

Many respondents considered that it would be useful to have additional guidance on the allocation of goodwill to CGUs. In particular, these respondents considered that:

- additional guidance on the allocation of goodwill to CGUs would have the benefit of giving more direction and discipline to preparers;
- the current model in IAS 36 gives incentives to companies to allocate goodwill to the CGUs that have a bigger pre-acquisition headroom or to undertake an organisational restructure to avoid goodwill impairments;

- there is need for an allocation basis that works reasonably well and does not heavily depend on management subjective views; and
- additional guidance could help management applying its judgement to arrive at the most appropriate allocation approach.

Nonetheless, a few respondents recalled that a key principle in IAS 36 is that goodwill shall be allocated to a CGU that is expected to benefit from the synergies of the business combination. Thus, determining an appropriate allocation method will always involve management judgement and different allocation methods may be acceptable.

By contrast, a number of respondents did not support EFRAG's discussion on additional guidance on the allocation of goodwill. These respondents argued that:

- IAS 36 already enables an entity to use its judgment to determine an appropriate method to allocate goodwill to the CGUs, which is key for faithful presentation of the economics of the transactions, and that this judgement subsequently reviewed by auditors;
- the discussions on goodwill allocation are more related to the general nature of goodwill and should be addressed within a "wider and longer term project on goodwill accounting"; and
- the difficulty in allocating goodwill is a consequence of the complex structure of groups and problems on identifying synergies that cannot be easily solved by standard-setting means.

Some of these respondents also criticised EFRAG's suggestions as they:

- seemed to constitute a rule-based approach which would not necessarily lead to an appropriate allocation of goodwill;
- seem to be driven by anti-abuse concerns with the aim of avoiding opportunistic allocations of goodwill and having early impairments;
- seemed to be costly and burdensome to implement without leading to significant improvements; and
- did not seem to fit the objective of simplification of the impairment test.

Allocation methods

When specifically referring to the suggestion that the allocation of goodwill may be based on the pre- and post-acquisition fair value of each CGU (or group of CGUs) that is expected to benefit from the acquisition (**example included in paragraph 2.10**), respondents expressed the following views:

- a number of respondents acknowledged the potential benefits of the example included in paragraph 2.10 of the DP. One respondent further detailed that this example was broadly aligned with the methodology applied by valuation practitioners when performing a goodwill allocation. One other respondent noted that this example had the advantage addressing a wide range of circumstances, including those where the benefits from the business combination are expected to be realized by CGUs to which no acquired assets and liabilities are assigned;

- one respondent highlighted the costs of such an approach as pre- and post-acquisition fair values of CGUs are usually not readily available; and
- one respondent pointed out that the example included in the DP did not explicitly demonstrate how the allocation should be done to a CGU that is only indirectly affected by the business combination (i.e. no assets have been assigned to the CGU). This respondent suggested including a third CGU to address this issue.

When specifically referring to EFRAG's suggestion that entities could be allowed to allocate the goodwill on the basis of the difference between the fair value of the portion of the acquired business to be included in a CGU and the fair value of the net assets of the acquired business that have been assigned to a CGU for additional guidance on the allocation of goodwill (**example included in paragraph 2.12**):

- a number of respondents expressed concerns for such an approach as it would not be aligned with the principle in paragraph 80 of IAS 36 that goodwill shall be allocated to the CGUs that are expected to benefit from the synergies of the business combination, irrespective of whether other assets or liabilities of the acquiree are assigned to those CGUs;
- one respondent preferred the second example because it would be easier to calculate the fair value of the parts of the acquired business than pre and post-acquisition fair value of the CGUs; and
- one respondent believed that this approach could be applied in a narrower set of circumstances and noted that practitioners often use this approach.

Finally, some respondents provided more general comments over the different allocation methods suggested in the DP. For example:

- the allocation methods proposed in the DP could become part of the illustrative and non-mandatory guidance accompanying IAS 36. Nonetheless, the illustrative examples should be clearer and the DP should explain the conceptual basis behind each illustrative example;
- the examples provided are relatively simple since they related only to the initial allocation and do not deal with the complex evolutions in a group's structure; and
- any new additional guidance on the allocation of goodwill should be principle-based and should provide information about the rational used.

Allocation ceiling

A few respondents appreciated the idea of an 'allocation ceiling', described in paragraph 2.13 of the DP, in which the amount of goodwill allocated to a CGU should not exceed the expected synergies.

However, most of the respondents that referred to the allocation ceiling were concerned that such an approach could increase the costs and add complexity to the goodwill impairment requirements. One respondent emphasised that currently companies were not required to measure the pre- and post-acquisition headroom of a CGU. One other respondent considered that the allocation ceiling should not

be introduced independently of other aspects of the modifications proposed since it would be burdensome. To overcome the cost issue, one respondent suggested the introduction of a cost-benefit assessment.

Finally, one respondent acknowledged that the pre-acquisition headroom of a CGU could decrease if the goodwill is misallocated or when a portion of the acquired goodwill arises from overpayment. However, this respondent considered that overpayments were infrequent and that it was premature to set out a principle of how to address the issues related to the pre-acquisition headroom as the IASB had not yet finalised its proposals.

Additional disclosures

A number of respondents acknowledged that a reconciliation of the total goodwill allocated to each CGU could provide useful information to users of financial statements about the origin of the impairment and the success of each business combination. In particular, one user representative group complained that CGUs were defined by management in a process that was subjective and not disclosed and this undermined the credibility of the impairment test as management could manipulate the CGUs to avoid impairment.

However, most of the respondents that referred to EFRAG's suggestion on the additional disclosures highlighted that it would be difficult and onerous to track and assess each individual component of goodwill over time, particularly when there are reorganisations, mergers or a sale of parts of CGUs.

Some of these respondents even questioned the usefulness and practicability of the information relating to the composition of goodwill and generally disagreed with the suggestion to include additional disclosures.

Finally, when referring to EFRAG suggestions more in general, some respondents invited EFRAG to:

- better explain how the reconciliation should be carried out over time, particularly when there is a restructure or an impairment;
- contemplate additional disclosures only after extensive consultations with users and preparers;
- ensure consistency with the IASB's Better Communication project; and
- make a cost-benefit analysis for such disclosures.

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

Some respondents, mainly users' professional organisations, provided alternative views and suggestions on how to improve the allocation of goodwill. For example:

- the allocation of goodwill should be determined based on the deal projections, including the synergies expected from the business combination along with where they are expected to be realised. This approach could meet both the improvement and simplification objectives that EFRAG has referenced;

- the IASB should require disclosures on the composition of the CGUs, especially if there are changes on their composition, to help investors better understand how changes in the composition of CGUs may influence the results of the goodwill impairment test;
- if goodwill is impaired, then an entity should disclose the cumulative value of goodwill impaired so that investors can see how much has been invested over time;
- the IASB should focus on disclosures on the basis of how the goodwill is calculated and the net identifiable assets recognised;
- EFRAG should further analyse ‘allocation methods based on different underlying economics of the goodwill’;
- entities should be required to make an impairment test before making reallocations of goodwill; and
- the IASB could prohibit the allocation of goodwill to a group of CGUs.

One respondent noted that paragraph 80 of IAS 36 requires goodwill to be tested at the lowest level at which it is monitored for internal management purposes, which cannot be higher than an operating segment. However, this respondent noted that in practice, many entities do not monitor goodwill on an ongoing basis and therefore may default to the level of the operating segment when performing the annual impairment test. This respondent considered that the wording of this paragraph should be improved and refer to the monitoring of the performance of the CGU to which goodwill is allocated. Similarly, one national standard setter considered that the principle of ‘the lowest level at which the goodwill is monitored for internal management purposes’ is rather vague. This may lead to diversity in practice in identifying the applicable CGU level and called for improvements in this respect.

Question 2 - When an entity should determine the recoverable amount

In paragraphs 2.23 to 2.37 of Chapter 2 EFRAG discusses the introduction of a qualitative assessment (‘Step Zero’) to the impairment process.

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

Support for the introduction of the Step Zero approach

The majority of the respondents generally welcomed the introduction of an option to perform first a qualitative assessment of the likelihood of an impairment (‘Step Zero’).

A number of respondents noted that the requirements in IAS 36 for the calculation of the recoverable amount are complex, costly and have to be performed at least annually even if there is no indication of an impairment and the CGU has a significant headroom. One respondent explained that the calculation of the recoverable amount was often performed for documentation purposes and added no value.

Respondents acknowledged that paragraph 99 of IAS 36 already provided a practical exception and allowed entities to use of the most recent detailed calculation of the recoverable amount as a test for the current period. However, some noted that such exception was rarely used as it was subject to strict conditions.



In general, those that expressed support for the Step Zero highlighted that its introduction would:

- represent a simplification and reduce costs for preparers;
- eliminate one of the existing differences between the IFRS and US GAAP requirements on goodwill impairment;
- be in line with the principle of materiality and provide entities a relief of a full impairment test when the potential negative impact is not material; and
- provide a relief that is less restrictive than paragraph 99 of IAS 36 and can be applied more broadly.

When referring to the suggestions included in the DP in more detail, respondents were mainly worried about the high threshold for the relief, having additional disclosures, the level of judgement involved and the risk of abuse. In particular, respondents considered that:

- if the relief only encompasses cases where the likelihood of impairment is remote, then the Step Zero approach might not reduce significantly the costs for preparers. Thus, it may be more operational to have a lower likelihood threshold;
- if the Step Zero is combined with extensive disclosure requirements, the objectives of an overall simplification and reduction of costs will not be achieved;
- the qualitative assessment should be properly designed to ensure consistent application and enforceability; and
- it is uncertain whether performing a qualitative assessments based on judgments and assumptions that would be discussed with an auditor could truly constitute a relief for entities compared to the quantitative test.

Finally, those that supported the Step Zero approach provided a number of suggestions:

- there is a need to reach an harmonised solution for both IFRS and US GAAP on the likelihood threshold;
- EFRAG should further evaluate, together with users and preparers, the effectiveness of the Step Zero in terms of cost reduction and producing relevant information. For example, EFRAG should further analyse the US experience with the existing qualitative assessment under US GAAP;
- the Step Zero should be accompanied by a periodic mandatory impairment test (e.g. every 3 years);
- the Step Zero should only be allowed after a first full impairment test. The qualitative assessment would be a way of monitoring of the different parameters used for the first impairment test;
- the IASB could still first revisit the criteria in paragraph 99 of IAS 36 to allow greater use of the exception before considering the introduction of the Step Zero;

- goodwill-oriented indicators described in the DP should be evaluated altogether but should not be all inclusive and could be also be useful as impairment indicators;
- the “acid test” mentioned in the DP could be one of the factors that may receive more weight, rather than triggering automatically a quantitative test;
- clear disclosure of the sensitivity of key assumptions could be helpful;
- EFRAG should add one macroeconomic indicator: “a significant rise, or change of benchmark, of risk free rate or of country risk factor that was used to assess the discount rate”.
- the Step Zero approach should not be introduced without considering its effect on all intangibles with indefinite life and any change in the impairment requirements of goodwill should also apply to all intangibles with infinite life; and
- incorporating discrete quantitative decline thresholds for revenue or other financial metrics as an impairment indicator may result in prescriptive guidance.

No support for the Step Zero

By contrast, a number of respondents, notably professional organisations, did not fully support the introduction of a Step Zero. In general, these respondents considered that introduction of Step Zero would not reduce significantly the costs for preparers and, most importantly could result in delays on the recognition of goodwill impairments. More specifically, these respondents noted that:

- the Step Zero would not significantly reduce the operational costs of the impairment-only approach and could even introduce additional complexity and operational costs without clearly demonstrating benefits;
- the introduction of Step Zero could delay the recognition of impairment value;
- compulsory impairment test is a good management tool to monitor the performance of the acquisition;
- the annual impairment test helps preparers maintaining the competencies required to perform a complex exercise and ensuring that the data-collection mechanism functions properly;
- a judicious application of the principle of materiality should permit entities to avoid carrying out a test when the potential negative impact is very small; and
- the threshold prompting the impairment test under US GAAP is different from what EFRAG is proposing, thus both requirements will not be fully converge.

Nonetheless, some of these respondents considered that it would be worth to explore the introduction of the Step Zero. They considered that the Step Zero could be an option available to entities in some relevant circumstances but it needed to be robustly written. Furthermore, EFRAG should analyse the application of the qualitative assessment that exists in the US GAAP, particularly in terms of cost-benefit analysis and the effects on the timeliness of the impairments.

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

One respondent considered that the IASB should instead revisit the criteria in 99 paragraph of IAS 36 to provide some relief to preparers.

Question 3 - How an entity should determine the recoverable amount

In paragraphs 2.38 to 2.78 of Chapter 2 EFRAG discusses how an entity determines the recoverable amount. IAS 36 currently defines the recoverable amount of the CGU as the higher of its FVLCD and VIU.

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

Most of the respondents that replied to this question did not support the introduction of a single method for determining the recoverable amount. These respondents claimed that:

- a single method for determining the recoverable amount would not result in a significant operational relief or real simplification as currently entities are not required to calculate both the VIU and FVLCS;
- it is important to maintain consistent requirements for all the assets under the scope of IAS 36 and challenged the introduction of a single method calculation for goodwill impairment purposes without having a broader discussion on other intangible assets with infinite life;
- both VIU and FVLCD can provide useful information and eliminating of one of the two methods would lead to a too narrow approach;
- no preference should be given to the market's expectation of the recoverable amount of an asset over a reasonable estimate performed by the individual enterprise that owns the asset;
- the FVLCD method is relevant and can be used as a benchmark or to test the reasonableness of the VIU, particularly when the VIU indicates an impairment;
- the elimination of one method would constitute an important change to fundamental principles of IAS 36.

Finally, some of these respondents considered that it would be useful to have more:

- guidance on the differences between the FVLCD and VIU in order to clarify their application and differences on the results;
- guidance on how the VIU should be calculated;
- disclosures to explain the rationale behind the choice of the method used for determining the recoverable amount and keep the same method over time; and
- disclosures regarding the fair value assessment which would allow users to better assess the valuation.

By contrast, some respondents welcomed EFRAG's suggestion to consider a single calculation approach for the recoverable amount. These respondents considered that:

- there is diversity in practice on the use of VIU and FVLCD;
- in most circumstances the VIU and FVLCD are expected to be similar;
- a single measurement approach based on assumptions used in the business plan of the management could allow a better information communicated to users; and
- the application of one method will be more reasonable and understandable, particularly when considering that the VIU and FVLCD are not based on the same assumptions, which leads to complexity.

One of these respondents considered that having a single calculation approach was a significant change to the fundamental principles of IAS 36. Thus, EFRAG should further discuss whether such change is needed on all other assets that are under the scope of IAS 36.

One other also called for more guidance on the differences between the FVLCD and VIU in order to clarify their application.

Preferred method

When referring to the preferred method, many respondents considered that the VIU was the most appropriate method to calculate the recoverable amount because it reflects the way management expects to extract value from the CGUs. Many of these respondents considered that the VIU should be retained if a single method was to be introduced.

Two respondents, that supported a single method for calculation of the recoverable amount, provided different views on what is the best method to calculate the recoverable amount:

- One respondent would support a model using post-tax cash flows and post-tax discount rate, with clear guidance on the calculation of reasonably supportable cash flows, without IAS 36 restrictions on restructuring and enhancement cash flows;
- One other respondent considered the FVLCD the best method as it provides the most relevant information about the performance of a CGU, it is easier to apply and consistent with the basis on which goodwill and other intangibles were initially recognised.

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

Most of the respondents supported EFRAG's suggestion to allow entities to incorporate the effect of planned future restructurings (inflows and outflows) into the cash flow projections, even when the threshold to recognise a provision for restructuring costs has not yet been met. These respondents considered that the existing constraints in IAS 36 are too restrictive and the inclusion of future restructurings could enhance the relevance of the impairment test as:

- the calculation of the VIU would reflect management assumptions and how it intends to run the business;
- the estimation of future cash flows would reflect the elements considered by the acquirer when determining the acquisition price, including future restructurings; and
- it would reduce costs since entities would have to build one single business plan of the CGU for management and impairment purposes.

Nonetheless, some respondents noted that they would support the inclusion of future restructurings in the calculation of the VIU to the extent that:

- future restructurings have been approved by management and this should be a requirement under IAS 36;
- future restructurings are reliable for market participants;
- future/planned investments are also considered; and
- IAS 36 includes some constraints on the use of future restructurings and future investments such as those described in paragraph 2.51 of the DP or, for example, limiting their use to the first 3 years of the management's financial budget/forecast.

Finally, a few respondents were not supportive about reflecting future restructurings in the calculation of the VIU in use because:

- it would represent a significant change to IAS 36, particularly on the definition of the VIU; and
- it would result in greater alignment between the FVLCD and VIU.

Even so, one of these respondents considered that on balance it may be useful to reflect future restructurings on the calculation of the value because of the special nature of goodwill as an aggregate item and the prohibition of reversing an impairment loss.

One respondent considered that this point must be linked to whether to maintain two valuation methods or eliminate one of them. If one valuation method is eliminated, the one remaining should include future restructurings. However, the coherence of the valuation of the future restructuring and the timing of the accounting for the restructuring provision must be also analysed.

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

Almost all respondents supported EFRAG's suggestion that IAS 36 should be changed to allow entities an election between a pre-tax or post-tax calculation with use of a post-tax discount rate in the calculation of the value in use. These respondents explained that:

- entities often conduct the impairment tests on a post-tax basis with an additional iteration performed simply to derive a pre-tax discount rate;

- the introduction of a choice would simplify the calculation of the VIU and reduce costs, particularly when entities only have observable post-tax discount rates for an asset/CGU and it is difficult to calculate an appropriate pre-tax rate;
- here is no clear advantage of one or the other method because both (pre-tax and post-tax) calculations should lead to the same value in use; and
- the requirement to conduct the test on a pre-tax basis and the related requirement to exclude the effect deferred tax assets and deferred tax liabilities in the determination of the carrying value of the CGU introduces unnecessary complexity and may produce unintended results.

Moreover, some respondents emphasised some additional aspects that need to be considered if entities are allowed to make an election between a pre-tax or post-tax calculation. In particular, it is important to:

- ensure consistency between the discount rate, the cash flows used and the book value of the CGU, including the effects of deferred taxes. Additional guidance may be needed to ensure this consistency; and
- require disclosures about the discount rate used by the entity and the reasons for its choice, particularly when using a pre-tax discount rate.

One preparer noted that the post-tax rate issue is only relevant to preparers that apply the weighted average cost of capital ('WACC') as a discount rate.

Finally, one standard setter was not convinced that the possibility to use of a post-tax calculation represented a simplification and led to a reduction of costs. This respondent explained that the use of post-tax rates would raise new questions. For instance, how should an entity adjust the future cash flows for tax consequences or how to reflect deferred taxes in the carrying amount of the CGU?

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

In general, respondents acknowledged that the basic assumption underlying the goodwill accretion approach and its objective. However, the majority of the respondents did not fully support EFRAG's goodwill accretion approach. These respondents:

- expressed concerns that the goodwill accretion approach would add complexity and subjectivity to the goodwill impairment model. For example, additional assumptions have to be made in order to determine the goodwill accretion rate, which will give rise to interpretation and application issues;
- if acquired goodwill is an asset that is being consumed and decreasing over time, then the discussion should then be focused on the reintroduction of goodwill amortisation, which is a simpler approach;
- the goodwill accretion approach is similar to the goodwill amortisation approach which assumes that the goodwill acquired in a business combination is being consumed over a period of time;

- the model would be difficult to communicate, both externally and internally, and therefore it will be hard to achieve acceptance and legitimacy for its outcome;
- the useful life of purchased goodwill is infinite as long as the expectations of the business plan on which the acquisition is based is achieved;
- difficult to distinguish future cash flows from the asset initially recognised from the future cash inflows from internally generated goodwill or a modification of an asset;
- the goodwill accretion seems to create a conflict with the general objective in IAS 36 as it is focused on reducing the value of goodwill more rapidly over time; and
- the application of a “notional interest expense” on the opening balance of goodwill does not seem to reflect the internally generated goodwill. Assuming that the management’s estimates of the future cash flows do not vary from one year to another (i.e. no goodwill is generated internally and the VIU of the CGU is maintained). According to the proposed “goodwill accretion method”, an impairment loss would be recognized whose relevance is highly questionable.

Two users representative associations acknowledged the challenges of the goodwill accretion approach, nonetheless considered that it could be a reasonable compromise to solve the issues related to internally generated goodwill and timeliness of impairments. To simplify the model, these respondents suggested that the discount rate could be fixed at the acquisition date.

One other respondent even if not expressing a view on the goodwill accretion approach, it noted that acquired synergies are consumed, but it is difficult to draw the line that separates the part attributed to the old value and to the new value from the recoverable amount.

One respondent noticed that the IASB was currently discussing a similar issue and that the IASB had not yet finalised its proposals. Thus, this respondent considered that it was important to evaluate the IASB’s proposals before exploring other approaches.

One other respondent considered that a short-term simplification project should not introduce new concepts such as goodwill accretion approach. Such improvements would be better suited in a more comprehensive project.

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

Some respondents referred to the IASB’s pre-acquisition headroom approach when replying to the questions included in the DP. Most of these respondents disagreed with the idea of removing the pre-acquisition headroom of a CGU for goodwill impairment purposes. These respondents argued that:

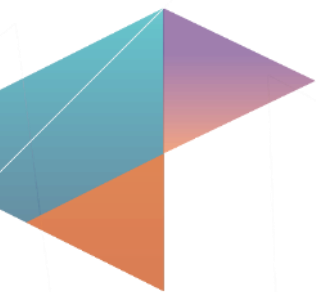
- such an approach would, as already mentioned above, introduce new concepts and should, therefore, be explored within a more comprehensive project;
- the IASB’s pre-acquisition headroom would increase the complexity of impairment testing since the goodwill from individual acquisitions and the individual impairments would have to be tracked in detail over time. One national standard setter questioned whether it would be feasible to apply this approach in cases of successive acquisitions.

- the headroom approach is just another attempt to make the distinction between acquired and internally generated goodwill with little conceptual basis; and
- there is no evidence that the decrease in the headroom relates to acquired goodwill rather than to pre-existing internally generated goodwill.

In addition, one respondent noted that the fact that standard setters' are discussing issues such as headroom goodwill and internally generated goodwill gives evidence that the assumption that goodwill has an indefinite useful life is flawed.

One respondent considered that when a business is a true going concern, goodwill should be on the statement of financial position forever unless the associated business is closed or sold. This would make it easier to assess returns over time, reduce the incentive for the incoming management to make impairments and simplify the accounting for goodwill.

Finally, one respondent concluded that the general underlying controversy on the right approach for goodwill accounting needs a compromise solution that is pragmatic from an operational perspective on the one hand, but still retains much of the relevant conceptual reasoning on the other hand. The respondent suggested that this could take the form of allowing an accounting policy choice between amortisation and the impairment-only approach with the appropriate disclosure.



APPENDIX – List of respondents

<i>Respondent</i>	<i>Country</i>	<i>Type</i>
Accountancy Europe	Europe	Business Association
ACTEO	France	Business Association
AFRAC - Austrian Financial Reporting and Auditing Committee	Austria	National Standard Setter
ANC - Autorité des Normes Comptables	France	National Standard Setter
ASCG - Accounting Standards Committee of Germany	Germany	National Standard Setter
BNP Paribas	France	Preparer
Business Europe	Europe	Business Association
CNC - Comissão Normalização Contabilística	Portugal	National Standard Setter
CRUF - The Corporate Reporting Users Forum		Professional Organisation of Users
DASB - Dutch Accounting Standards Board	Netherlands	National Standard Setter
Duff & Phelps		Professional Organisation of Users
EFFAS - European Federation of Financial Analysts Societies	Europe	Professional Organisation of Users
GDV - German Insurance Association	Germany	Business Association
ICAC - Instituto de Contabilidad y Auditoria de Cuentas	Spain	National Standard Setter
Insurance Europe	Europe	Business Association
KBC	Belgium	Preparer
Mazars	France	Auditing
Muhammad Hadidjaja		Individual Person
OIC - Organismo Italiano de Contabilità	Italy	National Standard Setter
PwC	UK	Auditing
SEAG - Swedish Enterprise Accounting Group	Sweden	Business Association
SFAF - French Society of Financial Analysts	France	Professional Organisation of Users