（Translation for reference purpose only）

Japan's Modified International Standards (JMIS): Accounting Standards Comprising IFRSs and the ASBJ Modifications

ASBJ Modification Accounting Standard No. 1

Accounting for Goodwill

30 June 2015
Amended 11 April 2018
Accounting Standards Board of Japan

Contents

Paragraph

（**Translation for reference purpose only**）

Objective

1. This Standard forms part of "Japan's Modified International Standards (JMIS): Accounting Standards Comprising IFRSs and the ASBJ Modifications". The objective of this Standard is to make 'deletions or modifications' to the Standards and Interpretations (collectively referred to as 'Standards') issued by the International Accounting Standards Board ('IASB') relating to the accounting for goodwill acquired in a business combination and the accounting for goodwill relating to an associate or a joint venture and related disclosures.

2. The basis for conclusions accompanies, but does not form part of, this Standard.

3. [This paragraph is not used for the English version.]

Accounting Standard

Accounting

4. 'Deletions or modifications' shall be made to the requirements regarding the accounting for goodwill acquired in a business combination in IFRS 3 *Business Combinations* in the following manner (new text is underlined and deleted text is struck through):

54 In general, an acquirer shall subsequently measure and account for assets acquired, liabilities assumed or incurred and equity instruments issued in a business combination in accordance with other applicable IFRSs for those items, depending on their nature. However, this IFRS provides guidance on subsequently measuring and accounting for the following assets acquired, liabilities assumed or incurred and equity instruments issued in a business combination:

(a) reacquired rights;

(b) contingent liabilities recognised as of the acquisition date;

(c) indemnification assets; ~~and~~

(d) contingent consideration; and~~.~~

J-(e) goodwill.

Paragraph B63 provides related application guidance.

Goodwill

J-58A The acquirer shall account for goodwill as follows:

(a) After initial recognition, goodwill shall be carried at the amount recognised at the acquisition date less any accumulated amortisation and any accumulated impairment losses.

(b) Goodwill shall be amortised on a systematic basis, using the straight line method or other reasonable method, over its useful life. The useful life of goodwill is the period for which goodwill is expected to have an effect, which shall not exceed 20 years. The amortisation charge shall be recognised in profit or loss.

(c) Amortisation of goodwill shall begin at the acquisition date.

(d) The amortisation method and the useful life for goodwill shall be determined separately for each business combination.

B63 Examples of other IFRSs that provide guidance on subsequently measuring and accounting for assets acquired and liabilities assumed or incurred in a business combination include:

(a) IAS 38 prescribes the accounting for identifiable intangible assets acquired in a business combination. ~~The acquirer measures goodwill at the amount recognised at the acquisition date less any accumulated impairment losses.~~ IAS 36 *Impairment of Assets* prescribes the accounting for impairment losses.

(b) IFRS 4 *Insurance Contracts* provides guidance on the subsequent accounting for an insurance contract acquired in a business combination.

(c) IAS 12 prescribes the subsequent accounting for deferred tax assets (including unrecognised deferred tax assets) and liabilities acquired in a business combination.

(d) IFRS 2 provides guidance on subsequent measurement and accounting for the portion of replacement share-based payment awards issued by an acquirer that is attributable to employees' future services.

(e) IFRS 10 provides guidance on accounting for changes in a parent's ownership interest in a subsidiary after control is obtained.

5. 'Deletions or modifications' shall be made to the requirements regarding the accounting for goodwill relating to an associate or a joint venture in IAS 28 *Investments in Associates and Joint Ventures* in the following manner (new text is underlined and deleted text is struck through):

32 An investment is accounted for using the equity method from the date on which it becomes an associate or a joint venture. On acquisition of the investment, any difference between

the cost of the investment and the entity's share of the net fair value of the investee's identifiable assets and liabilities is accounted for as follows:

(a) Goodwill relating to an associate or a joint venture is ~~included in the carrying amount of~~ not presented separately with the investment. ~~Amortisation of that goodwill is not permitted.~~ An entity shall account for goodwill relating to an associate or a joint venture as follows:

(i) Goodwill relating to an associate or a joint venture shall be amortised on a systematic basis, using the straight line method or other reasonable method, over its useful life. The useful life of goodwill is the period for which goodwill is expected to have an effect, which shall not exceed 20 years. The amortisation charge shall be recognised in profit or loss.

(ii) Amortisation of goodwill relating to an associate or a joint venture shall begin at the time when an investee becomes an associate or a joint venture.

(iii) The amortisation method and the useful life for goodwill relating to an associate or a joint venture shall be determined separately for each investment in an associate or a joint venture.

…

40 After application of the equity method, including recognising the amortisation charge for goodwill relating to an associate or a joint venture in accordance with paragraph 32 and recognising the associate's or joint venture's losses in accordance with paragraph 38, the entity applies paragraphs 41A-41C to determine whether there is any objective evidence that its net investment in the associate or joint venture is impaired.

42 ~~Because goodwill that forms part of the carrying amount of the net investment in an associate or a joint venture is not separately recognised, it is not tested for impairment separately by applying the requirements for impairment testing goodwill in IAS 36 *Impairment of Assets*. Instead,~~ For a net investment in an associate or a joint venture, the entire carrying amount of the investment is tested for impairment in accordance with IAS 36 as a single asset, by comparing its recoverable amount (higher of value in use and fair value less costs to sell) with its carrying amount whenever application of paragraphs 41A-41C indicates that the net investment may be impaired. ~~An impairment loss recognised in those circumstances is not allocated to any asset, including goodwill, that forms part of the carrying amount of the net investment in the associate or joint venture. Accordingly, any~~

~~reversal of that impairment loss is recognised in accordance with IAS 36 to the extent that the recoverable amount of the net investment subsequently increases.~~ In determining the value in use of the net investment, an entity estimates:

…

J-42A An impairment loss for a net investment in an associate or a joint venture shall be allocated first to any remaining goodwill relating to the associate or the joint venture.

J-42B After the recognition of an impairment loss, the amortisation charge for goodwill relating to an associate or a joint venture shall be adjusted in future periods to allocate the goodwill's carrying amount to which the impairment loss was allocated in accordance with paragraph J-42A on a systematic basis over its remaining useful life.

J-42C The increased carrying amount of a net investment in an associate or a joint venture attributable to a reversal of an impairment loss shall not exceed the carrying amount that would have been determined had no impairment loss been allocated to the net investment other than goodwill relating to the associate or the joint venture in prior years.

J-42D An impairment loss allocated to goodwill relating to an associate or a joint venture shall not be reversed in a subsequent period.

Disclosure

6. 'Deletions or modifications' shall be made to the requirements regarding disclosures relating to goodwill acquired in a business combination in IFRS 3 in a following manner (new text is underlined and deleted text is struck through):

B64 To meet the objective in paragraph 59, the acquirer shall disclose the following information for each business combination that occurs during the reporting period:

…

(e) a qualitative description of the factors that make up the goodwill recognised, such as expected synergies from combining operations of the acquiree and the acquirer, intangible assets that do not qualify for separate recognition or other factors.

J-(ea) the amortisation method and the useful life (or lives) adopted for goodwill and the line item(s) in the statement of profit or loss and other comprehensive income that include the amortisation charge for goodwill.

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…

B67 To meet the objective in paragraph 61, the acquirer shall disclose the following information for each material business combination or in the aggregate for individually immaterial business combinations that are material collectively:

…

(d) a reconciliation of the carrying amount of goodwill at the beginning and end of the reporting period showing separately:

(i) the gross carrying amount and accumulated ~~impairment losses~~ amortisation (aggregated with accumulated impairment losses) at the beginning of the reporting period.

(ii) additional goodwill recognised during the reporting period, except goodwill included in a disposal group that, on acquisition, meets the criteria to be classified as held for sale in accordance with IFRS 5 *Non-current Assets Held for Sale and Discontinued Operations*.

(iii) adjustments resulting from the subsequent recognition of deferred tax assets during the reporting period in accordance with paragraph 67.

(iv) goodwill included in a disposal group classified as held for sale in accordance with IFRS 5 and goodwill derecognised during the reporting period without having previously been included in a disposal group classified as held for sale.

(v) impairment losses recognised during the reporting period in accordance with IAS 36. (IAS 36 requires disclosure of information about the recoverable amount and impairment of goodwill in addition to this requirement.)

J-(v-a) any amortisation charge recognised during the period.

(vi) net exchange rate differences arising during the reporting period in accordance with IAS 21 *The Effects of Changes in Foreign Exchange Rates*.

(vii) any other changes in the carrying amount during the reporting period.

(viii) the gross carrying amount and accumulated ~~impairment losses~~ amortisation (aggregated with accumulated impairment losses) at the end of the reporting period.

…

Effective Date

7. An entity shall apply this Standard as issued in June 2015 (the ‘2015 Standard’) to consolidated financial statements for annual periods ending on or after 31 March 2016. Regarding quarterly financial reporting, an entity shall apply this Standard to consolidated interim financial statements for quarters within annual periods beginning on or after 1 April 2016.

7-2. An entity shall apply this Standard as amended in April 2018 (the ‘2018 Amendments’) to consolidated financial statements for annual periods which IFRS 9 *Financial Instruments* (2014) (‘IFRS 9 (2014)’) listed in Appendix 1 of *Application of “Japan’s Modified International Standards”* as amended in Apil 2018 is first applied. Regarding quarterly financial reporting, an entity shall apply the 2018 Amendments to consolidated interim financial statements from the first quarter of that annual period.

Approval by the Board

8. The 2015 Standard was approved for issuance by all 12 Board members attending the 314th Board meeting of the Accounting Standards Board of Japan. The following Board members attended this Board meeting:

Yukio Ono (Chairman)
Takehiro Arai (Vice Chairman)
Atsushi Kogasaka (Vice Chairman)
Tomokazu Sekiguchi
Aiko Sekine
Yasuyuki Fuchita
Hisayoshi Masawaki
Kazuyuki Masu
Masao Yanaga
Katsuhito Yanagibashi
Minoru Yoshida
Hitoshi Watanabe

8-2. The 2018 Amendments were approved for issuance by all 9 Board members attending the 382nd Board meeting of the Accounting Standards Board of Japan. The following Board members attended this Board meeting:

Yukio Ono (Chairman)
Atsushi Kogasaka (Vice Chairman)
Yasunobu Kawanishi

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Ryota Yasui

Katsuhito Yanagibashi

Yoshio Yukawa

Minoru Yoshida

Kazutaka Yoneda

Hitoshi Watanabe

Basis for Conclusions

History of the project

9. The Accounting Standards Board of Japan (‘ASBJ’) started the endorsement process of International Financial Reporting Standards (‘IFRS’) in line with “The Present Policy on the Application of International Financial Reporting Standards (IFRS)” issued in June 2013 by the Business Accounting Council, an advisory body to the Financial Services Agency of Japan. The scope of the initial endorsement process covered the Standards issued by the IASB as at 31 December 2012.

10. In the initial endorsement process, based on the discussions at its Board meetings, the ASBJ decided to make ‘deletions or modifications’ to the Standards issued by the IASB relating to the non-amortisation of goodwill because the ASBJ determined that the thinking in IFRS is critically different from the fundamental thinking on accounting standards generally accepted in Japan (see paragraphs 11-32).

10-2. The 2018 Amendments did not make any ‘deletions or modifications’ regarding goodwill in the endorsement process, but the 2018 Amendments amended the wording of the requirements subject to ‘deletions or modifications’ in order to reflect the amendments to IAS 28 made by IFRS 9 (2014).

Basis for Conclusions of the 2015 Standard

Amortisation of goodwill acquired in a business combination (paragraph 4)

11. IAS 22 *Business Combinations* as revised in 1998 (‘IAS 22 (1998)’) required the amortisation of goodwill arising on acquisition over its useful life, with a rebuttable presumption that the useful life of goodwill will not exceed twenty years from initial recognition. IFRS 3 *Business Combinations* issued in 2004 (‘IFRS 3 (2004)’) superseded IAS 22 (1998) and prohibited amortising goodwill acquired in a business combination and instead introduced annual impairment testing for goodwill. In addition, IFRS 3 (2004) clarified the definition of the term ‘identifiable’ and introduced the contractual-legal criterion and the separability criterion for the separate recognition of intangible assets.

12. In developing IFRS 3 (2004), proponents for amortising goodwill generally argued the following (IFRS 3 (2004), paragraph BC139):

    (a) acquried goodwill is an asset that is consumed and replaced with internally genarated goodwill;

    (b) conceptually, amortisation is a method of allocating the cost of acquired goodwill over the period it is consumed and is consistent with the approach taken to tangible fixed assets; and

    (c) the useful life of acquired goodwill cannnot be predicted with a satisfactory level of reliability, nor can the pattern in which that goodwill diminishes be known. Nevertheless, systematic amortisation over an albeit arbitrary period provides an appropriate balance between conceptual soundness and operationality at an acceptable cost.

13. However, the IASB decided to prohibit amortising goodwill acquired in a business combination for the following reasons (IFRS 3 (2004), paragraphs BC140 and BC142):

(a) the useful life of acquired goodwill and the pattern in which that goodwill diminishes are generally not known. Straight-line amortisation of goodwill over an arbitrary period fails to provide useful information;

(b) 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, provided that an entity is able to maintain the overall value of goodwill (by, for example, expending resources on advertising and customer service). However, the IASB remained doubtful about the usefulness of an amortisation charge that reflects the consumption of acquired goodwill, whilst the internally generated goodwill replacing it is not recognised; and

(c) if a rigorous and operational impairment test could be devised, more useful information would be provided to users of an entity's financial statements.

14. In the discussions at the ASBJ and among Japanese constituents, both views for and against the non-amortisation of goodwill were heard.

15. Opponents of non-amortisation of goodwill argue that goodwill should be amortised, primarily for the following reasons:

(a) goodwill constitutes the cost paid to acquire the assets and liabilities of the acquiree in a business combination. Because the acquirer's profit after the business combination should be viewed as the excess recovered beyond the cost invested, goodwill should be amortised from the viewpoint of appropriately recognising in each period the income and the corresponding cost of the investment.

(b) assuming certain portions of goodwill represent excess earning power, the value of such power normally diminishes due to the competitive environment. Non-amortisation of goodwill neglects to account for such phenomenon.

(c) regarding the view described in paragraph 13(a) that the useful life of acquired goodwill is generally unknown, an entity should generally be able to estimate the useful life of goodwill because an acquirer typically decides to undertake the acquisition after diligent analysis of the acquiree. In addition, although some may argue that the pattern in which goodwill diminishes cannot be predicted reasonably, it would be more reasonable to amortise goodwill on a systematic basis over a certain period rather than adopting an approach that may not recognise the decrease in the value of goodwill at all in certain periods.

Furthermore, the difficulty in estimating the useful life or the pattern of amortisation or depreciation exists not only in accounting for goodwill, but also in accounting for tangible fixed assets. In fact, determining the useful life of a tangible fixed asset requires the consideration of many factors, including expected physical wear as well as technical obsolescence arising from changes or improvements in production. Moreover, the determination of the depreciation method also requires an entity to reflect the pattern in which the asset's future economic benefits are expected to be consumed by the entity.

(d) regarding the view described in paragraph 13(b), paragraph OB7 of the *Conceptual Framework for Financial Reporting* issued by the IASB states that general purpose financial reports are not designed to show the value of a reporting entity, which implies that the recognition of internally generated goodwill is not relevant for general purpose financial reporting. Although the view described in paragraph 13(b) rejects the amortisation of goodwill on the grounds of being inconsistent with the accounting treatment for internally generated goodwill, the accounting treatment for advertising costs and the subsequent measurement of goodwill acquired in a business combination are entirely different issues.

(e) regarding the view described in paragraph 13(c), the impairment test for goodwill cannot be considered a substitute for the amortisation of goodwill because they differ in their objectives in that the amortisation of goodwill focuses on the periodical allocation of costs whereas the impairment test of goodwill focuses on recoverable amounts. In addition, because the recoverable amount would inevitably include the value of internally generated goodwill arising after the business combination, impairment tests would sometimes fail to represent the decrease in the value of goodwill acquired in a business combination.

16. In addition to the reasons listed in paragraph 13, other constituents support the non-amortisation of goodwill for the following reasons:

(a) in considering the importance of ensuring equal footing with foreign entities in the accounting for business combinations, non-amortisation of goodwill is beneficial for entities; and

(b) some users analyse financial statements on the basis of free cash flows and ignore goodwill amortisation charges, which is a non-cash item. Accordingly, non-amortisation of goodwill would not affect the analysis undertaken by such users.

17. As a result of the discussions at its Board meetings, the ASBJ decided to make 'deletions or modifications' to the Standards issued by the IASB to require the amortisation of goodwill, because the thinking in IFRS not to amortise goodwill and the fundamental thinking on accounting standards

generally accepted in Japan to amortise goodwill are critically different, in the light of the significance on the determination of profit or loss after the business combination as described in paragraph 15.

18. When making the ‘deletions or modifications’ so that goodwill is to be amortised, one of the major issues was how to prescribe the determination of the useful life for the amortisation of goodwill. Possible methods of prescribing the determination of the useful life for the amortisation of goodwill included: (a) requiring amortisation over the period reasonably estimated as a period over which goodwill will have effect, without specifying any upper limit; (b) requiring amortisation over a specified useful life, but permitting a shorter or longer period if it can be justified; (c) requiring amortisation within a specified upper limit of the useful life for goodwill; (d) requiring amortisation within a specified upper limit of the useful life for goodwill, but permitting a longer period if it can be justified; (e) requiring amortisation over the period reasonably estimated as a period over which goodwill will have effect, but within a specified upper limit when such a period cannot be reliably estimated.

19. Regarding whether the upper limit of the useful life is necessary, the ASBJ considered it reasonable to set an upper limit for the useful life, given the difficulty in reliably estimating the period for which goodwill is expected to have an effect, especially when that period is long. Regarding the specific length of the upper limit, considering that setting a too short of a period would make it difficult to reflect economic reality, the ASBJ decided that the upper limit should be 20 years, by reference to the requirements in IAS 22 (1998) and existing Japanese accounting standards.

Amortisation of goodwill related to associates or joint ventures (paragraph 5)

20. To be consistent with the ‘deletions or modifications’ requiring the amortisation of goodwill acquired in a business combination, the ASBJ decided to make ‘deletions or modifications’ to IAS 28 to require goodwill related to an associate or a joint venture to be amortised in a consistent manner.

21. IAS 28 treats the entire investment in an associate or a joint venture as a single asset and does not separately recognise goodwill related to an associate or a joint venture. To be consistent with requiring the amortisation of goodwill related to an investment in an associate or a joint venture, this Standard takes the view that an investment in an associate or a joint venture consists of the goodwill portion and the remaining portion, which would be accounted for separately but presented together.

22. Accordingly, the ASBJ decided to make ‘deletions or modifications’ to the Standards issued by the IASB to require that impairment losses on a net investment in an associate or a joint venture should be, consistent with impairment losses on goodwill in IAS 36 *Impairment of Assets*, allocated first to goodwill related to the associate or the joint venture, and to prohibit the reversal of the impairment

losses allocated to goodwill.

Disclosure relating to the amortisation of goodwill (paragraph 6)

23. To be consistent with the ‘deletions or modifications’ requiring the amortisation of goodwill acquired in a business combination, the ASBJ decided to add disclosure requirements to provide users of financial statements with information about the amortisation of goodwill. Specifically, the ASBJ decided to require the disclosure of the amortisation method, the useful life (or lives) adopted for goodwill and the line item(s) in the statement of profit or loss and other comprehensive income in which the amortisation charge for goodwill is included. The ASBJ also decided to modify the disclosure requirements regarding the reconciliation of the carrying amount of goodwill at the beginning and end of the reporting period.

Other related issues

24. In connection with the decision to require the amortisation of goodwill acquired in a business combination, the ASBJ also considered whether to make ‘deletions or modifications’ relating to the following issues:

    (a) annual impairment test of goodwill;

    (b) identification of intangible assets acquired in a business combination; and

    (c) non-amortisation of intangible assets with indefinite useful lives.

Annual impairment test of goodwill

25. IAS 36 requires an entity to test goodwill for impairment annually (and more frequently if events or changes in circumstances indicate that it might be impaired). The ASBJ considered whether any ‘deletions or modifications’ should also be made to this requirement in conjunction with requiring amortisation of goodwill.

26. Some argued that if goodwill were to be amortised, the recoverability of goodwill should be tested only when there is an indication that it may be impaired, similar to the impairment of other types of assets under IAS 36, because the requirement of annual impairment test for goodwill is an exception as a consequence of not amortising goodwill. Nevertheless, the ASBJ decided not to make ‘deletions or modifications’ in relation to this issue in order to minimise ‘deletions or modifications’ to the extent

possible.

Identification of intangible assets acquired in a business combination

27. IFRS 3 states that an intangible asset acquired in a business combination is identifiable if it meets either the separability criterion or the contractual-legal criterion, and IFRS 3 requires an entity to recognise identifiable intangible assets separately from goodwill. The ASBJ considered whether any 'deletions or modifications' should also be made to this requirement in conjunction with requiring amortisation of goodwill.

28. Some argued that 'deletions or modifications' should also be made to the requirement to identify intangible assets acquired in a business combination for the following reasons:

    (a) it would be relevant to identify intangible assets separately from goodwill only when they have been considered in determining the consideration for the business combination, such as when acquiring those intangible assets was one of the purposes of undertaking the business combination; and

    (b) if goodwill were to be amortised, the identification of intangible assets would be less needed because the effect on profit or loss would be limited to the difference in the amount of amortisation caused by the difference in the useful lives of the intangible assets and goodwill.

29. Nevertheless, the ASBJ determined not to make 'deletions or modifications' on this issue in order to minimise 'deletions or modifications' to the extent possible.

Non-amortisation of intangible assets with indefinite useful lives

30. IAS 38 *Intangible Assets* prohibits an entity from amortising intangible assets with indefinite useful lives and IAS 36 requires an entity to test those intangible assets for impairment annually (and more frequently if events or changes in circumstances indicate that it might be impaired). The ASBJ considered whether any 'deletions or modifications' should also be made to this requirement in conjunction with requiring amortisation of goodwill.

31. Some argued that 'deletions or modifications' should be also made to non-amortisation of intangible assets with indefinite useful lives because distinguishing goodwill from intangible assets with indefinite useful lives (such as certain brands) would be difficult and, thus, amortising one but not the other might create structuring opportunities.

32. However, others argued that those intangible assets need not always be treated in a manner similar to goodwill because an intangible asset with an indefinite useful life would have been determined to have no foreseeable limit to the period over which the asset is expected to generate cash flows, based on

the analysis of all of the relevant factors, whereas goodwill is merely a residual. In the light of this view, the ASBJ decided not to make 'deletions or modifications' on this issue.

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