CL24

Association pour la participation des entreprises françaises à l'harmonisation comptable internationale

Mouvement des Entreprises de France
MEDEF

EFRAG
35 Square de Meeûs
B-1000 Brussels
Belgium

November 30, 2014

Dear Mrs Flores,

**Re: Discussion Paper on ACCOUNTING AND DISCLOSURE FOR GOODWILL**

Please find below our comments on the issues raised in the above mentioned research paper.

If you have any questions or need any further information, please do not hesitate to contact us.

Yours sincerely,

| ACTEO | AFEP | MEDEF |
|---|---|---|
| Patrice MARTEAU | François SOULMAGNON | Agnès LEPINAY |
| Chairman | Director General | Director of economic and financial affairs |

***Question 3***

*The DP suggests the need for improved guidance in a number of areas in IAS 36. Do you think that the IASB should improve and/or provide additional guidance in relation to:*

*(a) The methods to determine the recoverable amount of the goodwill;*
*(b) The application of the value-in-use method;*
*(c) The identification of cash-generating units and allocation of goodwill to each unit; and*
*(d) The choice of the discount rate.*

*If not, please indicate why. Please state any specific suggestions for improvements if you have.*

We would first make some comments on the interpretations of the different surveys as reported in paragraphs 93 and following:

- On the subject of the conclusion that goodwill impairment was either not recognised or recognised too late following the financial crisis of 2008 (paragraphs 94 & 95), we believe that it is quite proper not to react to the arrival of a crisis by an immediate impairment. This crisis initially affected banks primarily, and entities in other sectors could not possibly have forecast either the magnitude or the time-horizon of any impact of the crisis on their activities in a reliable manner during the first months or even first year of the crisis since the necessary data was not available for most sectors. Indeed, we would contend that to have impaired goodwill immediately on the basis of necessarily incomplete and uncorroborated assumptions would have been inappropriate and contrary to the principles of IAS 36. As an illustration of this in one industry, the oil price (WTI) fell from a high of around $130/bbl in mid 2008 to $45/bbl at the end of 2008. At this level much of the goodwill and productive assets in the industry would have been impaired. However, by the middle to end of 2009 the price was back up to around $80/bbl, which comfortably supported goodwill and asset values at the time. It would, in our view, have been quite improper to impair goodwill at that time on the easy assumption that the oil price was not going to recover. Finally, even when the data was available to allow cash-flow projections to be adjusted, the revised value in use could still in many instances allow the carrying values of goodwill to be supported for a few more years.

- On the subject of the conclusion that the impairment-only approach leaves significant room for managerial discretion(paragraph 93(a), we agree that the model is based on judgment and assumptions but we believe that this is inherent in the very functioning of the projected cash flows approach on which the impairment test is based. The oil price example above shows, in our view, that judgment based on experience and objectivity is essential to the relevance of the impairment test.

  We also feel that the debate is not so much about the recognition of an accounting impairment charge but is really about the requirement of users to have reliable indicators of the entity's future performance.
  Indeed, IAS 36, with its requirements for disclosures about CGU containing intangible assets with indefinite useful lives, is the only standard that leads to the provision of information about

projections of performance in the notes to financial. We therefore wonder what kind of information about future cash-flows it is possible and reasonable to provide without adversely affecting the confidentiality of business, and we also need to consider whether this information should be provided in the notes or elsewhere.

As far as the level of the guidance provided by IAS 36 for the performance of the impairment tests is concerned, we believe that the current level of guidance is sufficient. We believe that room should be left for judgment in order to ensure that the performance of the test reflects the way in which the management considers the performance of its acquired businesses and of its CGUs. One way to make these tests relevant and reliable, and thus to reinforce the user's confidence, would be to strengthen the link between IAS 36 provisions and the segment reporting.

Groups need a principle-based standard that aligns the accounting model with internal management, especially when they manage a very large number of CGUs and carry out numerous and frequent internal reorganizations. A strong link between the allocation of goodwill and internal management of performance can ensure that the data used for the impairment test will be available, relevant and reliable.

Concerning the information being sought by users about projected cash flows, we acknowledge that the sensitivity tests could be a good way to prepare the market for a probable degradation of performance. However, it is very difficult to present relevant sensitivity tests:

- Because of the complex interdependency of economic factors, sensitivity to a single key assumption calculated independently from all others does not provide a realistic outcome. For internal management purposes, entities use more complex models which combine several parameters. Nevertheless, it would be dangerous for the entity to communicate using these tools, since it would be at risk of presenting information, which could be considered misleading, and thus a cause for litigation, if the scenarios are not realised.

- Owing to the commercially-sensitive information these tests may reveal. Again, a closer link between IAS 36's disclosure and IFRS 8's segment reporting would allow for more transparent information about projected cash flows since segment performance during the period (and earlier periods) should help in establishing trends and identifying potential risks of deterioration.

This last topic raises the broader question of whether it is the role of the financial statements to provide forward-looking information and if so, of what type and at what level of detail.

***Question 4***

*The DP suggests a number of possible new disclosures about impairment testing for goodwill. Do you think that the IASB should consider improving requirements to:*

*(a) assist users in understanding the robustness of the modelling and the entity's current assumptions;*
*(b) provide confirmation of the 'reasonableness' of the entity's past assumptions; and*
*(c) assist users in predicting future impairment.*

First, we wish to emphasize that we agree with the general remarks made in paragraph 130 relating to the requirements for disclosures about impairment tests and we have already commented on some of them in our response to question 3.  We agree that:

- Explicit disclosure objectives would be useful;
- Some information may be better disclosed elsewhere in the financial reports;
- Entities should consider the level of detail necessary to the usefulness of the information; and
- The standard setter (and the regulator) should consider risks relating to disclosing sensitive information.

We have however some further comments about the objectives listed in paragraph 134

We do not believe, as a general principle, that information should be provided in the notes with the objective of providing tools for the user to challenge the robustness of the financial statements. It is clearly the responsibility of preparers (at the highest level in the hierarchy), auditors and regulators to ensure that financial statements are prepared in a sound and serious manner for all aspects of the statements, including the use of judgment and assumptions. Notes to the financial statements should not be an audit tool. Similarly, we therefore believe that disclosures should not be designed to permit users to "second-guess" management's impairment test.

We therefore believe that the first objective should not be "to assist users in understanding the robustness of the modelling and assumptions" but rather to assist them to understand how they have been determined and the choices the management had to make. That is why we acknowledge that it could be useful for users to obtain a better understanding of, for example, how discount rates were determined, and thus we are not opposed to the disclosure of some qualitative information on the inputs to the discount rate calculation as proposed in paragraph 143. However, the proposal in paragraph 144 goes much further and is more akin to an exercise in justification rather than an informative disclosure.

Regarding the second proposed objective, which is to "provide confirmation of the 'reasonableness' of the entity's past assumptions", we also believe this would be more of a proxy for "verification" unless it is clear that the exercise of reconsidering past assumptions is orientated only towards providing a better understanding of the current assumptions and to improving the reliability to predict future cash-flows.
It should also be noted that analysis of variances, as proposed in paragraph 146, may be neither available in a suitable form, nor relevant for entities which undergo frequent changes in the composition of their CGUs.

Finally, we agree with the third objective, that is, that of assisting users in predicting future impairment. We believe that one of the best ways to achieve this is to reinforce the link between the segment reporting and the CGU.

***Question 1***

*Do you agree that there should be a requirement to recognise goodwill as an asset and amortise it over subsequent periods? If so, do you support amortisation because:*

*(a) goodwill existing at acquisition date is consumed and replaced with internally generated goodwill over time, thus it should be allocated to subsequent periods as part of the cost of acquiring an entity;*

*(b) an impairment-only model is not sufficiently reliable due to the large use of assumptions in the impairment test (future cash flows, terminal growth rate and discount rate); or*

*(c) amortisation of goodwill, in addition to the impairment test, achieves an appropriate cost-benefit balance.*

We agree that goodwill is an asset and thus it should not be immediately written off through net income, and even less so against equity. For the rest, we believe that EFRAG should not, at this stage, be too categorical about the appropriate treatment.

Goodwill may arise because some “assets acquired” could not be recognized as an asset or would be recognised at a value different from that estimated by management. The relevance of the amortization of goodwill therefore depends on the nature of these assets. Some assets/goodwill may have a definite and determinable useful life and therefore make amortization relevant but, in other cases, goodwill is generated by an underlying asset with an indefinite useful life on the day of acquisition. Thus, perhaps the first step should be to re-examine how IFRS 3 might allow the appropriate assets to be recognized and for what appropriate value. Moreover, we believe that other components of the goodwill such as overpayments or overvaluation of the consideration paid are more likely to be recognized in net income as a result of the impairment testing process.

If goodwill were to be amortised, it should not, in our view, be on the basis of an arbitrary and uniform amortization period. As far as possible useful lives should reflect the economic environment of the entity and the specific circumstances and attributes of each acquisition.

Furthermore, although we acknowledge that a systematic amortization approach is likely to put less pressure on the impairment test and may address the perception that impairments are recognized too late and create pro-cyclical effects because of their significant amounts, we are not convinced that this approach will improve the information provided to users as we believe that a systematic amortisation may reduce the utility of the information provided to users to help them to assess stewardship.

We therefore believe that the accounting for goodwill is not a precise science and we cannot at this stage be limited to the binary choice: for or against depreciation.

Perhaps the solution that the FASB has found for private companies should be examined more closely, as it allows an option for each business combination between amortization and non-amortisation. We also suggest that the IASB consider the amendment to the goodwill impairment test required under

Topic 350 that permits all entities first to assess qualitative factors to determine whether it is more likely than not that the fair value of the cash generating unit is less than its carrying amount.