



European Financial Reporting Advisory  
Group (EFRAG)  
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BELGIUM

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Dear Chairman,

**Re: Discussion Paper: Should Goodwill still not be amortised? Accounting and Disclosure for Goodwill**

BUSINESSEUROPE welcomes the opportunity to comment on the EFRAG Research Group's paper on the Accounting and disclosure for goodwill (the DP). Our comments below are made in the context of current accounting and disclosure for goodwill in the body of IFRS.

**Question 1**

***Do you agree that there should be a requirement to recognize goodwill as an asset and amortise it over subsequent periods?***

Is goodwill an asset?

In IFRS 3, "core goodwill" is defined as including two elements: the "going concern" element representing the ability of the acquiree's established business to earn a higher rate of return from the collection of net assets than would be expected if those net assets had to be acquired separately by the acquirer; and the synergies and other benefits expected from the combination of the acquiree's and the acquirer's net assets and businesses. In addition, any over- or underpayment resulting from the bidding process or a distress sale is also included in the carrying amount of the goodwill recognised, on the grounds that it is difficult to identify and reliably measure these elements at the time of the initial business combination.

There is widespread agreement amongst our members that acquired goodwill, including all the elements referred to above, is an asset and should be recognised as such. We agree with the conclusions IFRS 3.BC322 and 323 in this respect.

Should goodwill be amortised?

A majority of members are in favour of the amortisation of goodwill. This view is based on the reasons cited in paragraphs 13 and 75 of the DP:

- a) Acquired goodwill is an asset that is consumed over time, particularly in a competitive environment, and is replaced by internally generated goodwill over time. Amortisation ensures that acquired goodwill is recognised in profit or loss and not compensated for by the recognition of internally generated goodwill.
- b) Even though it may be difficult in some instances to estimate the useful life of goodwill, that is also the case for many items of property, plant and equipment or intangible assets. Amortisation is necessary to reflect this economic phenomenon and to attempt to match the consumption of the costs and the benefits of the transaction. Amortisation is consistent with the approach taken for other intangible and tangible assets that do not have indefinite useful lives, and there is no conceptual reason for treating acquired goodwill differently.
- c) Amortisation provides a practical solution for the subsequent accounting for goodwill, in that it obviates the need for a systematic and recurrent impairment test, which companies generally find onerous and of no use for internal management purposes.

Most members believe that it is possible to estimate the useful life of goodwill on a sufficiently reliable (or reasonable) basis using the economic assumptions that were used to price the transaction originally.

Finally, some members think that the allowing of the amortisation of goodwill would provide relief from the burden and consequent cost of searching for and measuring the acquiree's unrecognised intangibles which are currently required to be recognised and amortised separately from goodwill.

In contrast, some members consider the "impairment-only" approach to be more conceptually robust and more relevant to financial statements than the "amortization and impairment approach". They argue that the goodwill initially recognised is in some instances not replaced by internal goodwill but is rather sustained by rationalisation activity and future investment. In addition, there are some items acquired that often cannot be recognised separately as assets but which are of potentially indefinite life, such as, for example, synergies or access to a new market. It is also arguable a whether a premium paid to secure an acquisition is an asset, and its economic life is certainly impossible to assess. Moreover, the cessation of amortisation at the end of the economic life of goodwill can lead to a significant step-up in net profit which is difficult to link to a real economic event. In the view of these members, the best way to resolve such issues is to include these elements in goodwill and test them systematically for impairment.



However, the impairment test requires a lot of judgment (in respect of the definition of CGUs, preparation of future cash flow projections, calculation of the cost of capital, etc.), and the practical problems can outweigh the intended benefits. The information generated from annual impairment testing is not generally of use to management, can result in disclosures of competitive-sensitive information and is seen as an administrative burden.

On balance, we suggest that the following approach would be reasonable: there should be a rebuttable presumption that acquired goodwill has a finite useful life which the entity can estimate sufficiently reliably. Goodwill should be amortised over this period. Where the entity can demonstrate on a continual basis that goodwill has an indefinite useful life, or that the useful life cannot be estimated reliably, the entity should be required to apply an “impairment-only” approach as at present.

### **Question 2**

***Assuming that there was a requirement to amortise goodwill, do you think that the IASB should:***

- (a) Indicate what the amortization period should be?***
- (b) Indicate a maximum amortization period?***
- (c) Provide guidance on how entities should assess the amortization period (for instance, by referring to the expected payback period or the useful life of the primary asset)?***
- (d) Allow entities to elect the amortization period they consider appropriate?***

We note the findings of the academic research cited in paragraph 80 of the DP which indicate that the economic life of the “excess earning power” may generally be on average 10 years or less. However, we do not believe that a standard setter is better placed than the entity’s management to judge the useful life of any specific asset owned by the entity, including goodwill. Any imposition of a prescribed or maximum amortisation period would, in our view, be merely an “anti-abuse” measure, and as such, would have, in our view, no place in an accounting standard. We think that, over time, “market forces” (the scrutiny of users and regulators) will ensure that entities will not use unreasonable estimates.

We think that the entity’s management is able to arrive at a reasonable estimate of the useful life of acquired goodwill, and that the role of the standard setter should be limited to providing guidance on the factors that should be taken into account by the management in arriving at its estimate of useful life. In this respect, the suggestions laid out in paragraph 84 of the DP would provide a reasonable basis for the estimation of the amortisation period. Factors listed to be taken into account could include academic studies, such as those referred to in the DP.

In conclusion, we would support approaches (c) and (d) above. It is, of course, necessary for the amortisation approach to be complemented by a sound impairment model.

### **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 model;***
- (c) the identification of cash-generating units and allocation to each unit; and***
- (d) The choice of the discount rate.***

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

Although members recognise that they encounter difficulties and restrictions with the current model in the areas cited in the DP, they have developed approaches which they believe satisfy the requirements of the current standard and appropriately reflect the circumstances of their specific activities.

Many entities indicate that goodwill is not monitored at a very detailed level by management and that users do not appear to examine the allocation of goodwill in detail nor consider the subsequent accounting for goodwill closely. Although we can understand that users might react to a greater extent and more negatively to impairments that occur during a financial crisis, we are not convinced by the findings of the studies cited in paragraphs 94 to 96 which imply that depression in the financial markets should lead to an increase in goodwill impairment losses for industries other than the financial industry.

Consequently, we do not believe that it would be helpful or justified from a cost/benefit standpoint to provide further detailed guidance in IAS 36. We are concerned that any attempt to reduce the use of judgement by management will lead to a decrease in the entity-specific quality of impairment testing which will not enhance meaningful comparability.

The use of the pre-tax discount rate is contested by some on conceptual grounds, and is found to be very difficult to calculate. The question of the choice of the discount rate is a recurrent, widespread and difficult issue. The approach to the discount rate should be dealt with by the IASB on a holistic basis covering all areas where discounting is required in IFRS.

Finally, we agree with the conclusion of the DP (paragraph 100) that it is impractical to carry out an impairment test which considers only acquired goodwill. Entities that have considered this approach have found it to be extremely difficult to put into practice on a sustainable basis.

#### **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.***

The current disclosure requirements of IAS 36 in respect of goodwill are extensive and onerous to provide, and in some cases require information of a commercially-sensitive nature. While we recognise that some users complain of a lack of necessary information, we would caution the IASB against imposing any further requirements for disclosure without careful consideration and convincing justification of what is required and elimination of information which is not essential. This is an area where close cooperation between the standard setter, users and preparers would be required to arrive at an optimal set of requirements.

On the specific point raised in (b) above, we think that any requirement to justify the reasonableness of assumptions "after the event" would be both very onerous for preparers and create an increased risk of litigation for them. Although entities generally carry out analyses of variances as part of their normal performance reporting activity, such analysis is not specifically directed at the confirmation of assumptions for the goodwill impairment test. A requirement to prove the reasonableness of the assumptions used would be burdensome. Assumptions used for the impairment test should be consistent with those used for performance reporting and planning. We think it is the role of the entity and its auditors to ensure that the assumptions used for the test are reasonable and consistent, and the financial statements should at most have a statement to confirm that this is the case.

#### **Question 5**

***IAS 38 requires that intangible assets with indefinite useful lives are not amortised but tested for impairment at least annually. Assuming that there was a requirement to amortise goodwill, do you think that the same requirement should be extended to other intangible assets with indefinite useful lives? In addition, assuming that there was a requirement to amortise goodwill, do you think that the current requirements of identifying intangible assets separately from goodwill should be reconsidered? If so, how?***

In some cases (e.g. brands and trademarks) an indefinite useful life is certainly possible and the identification of the intangible asset and the valuation thereof is relatively straightforward. However, in other cases it would be reasonable to apply the same approach as that for goodwill, i.e. to use a rebuttable presumption as discussed in our response to Question 1.



In respect of the identification of intangible assets separately from goodwill, it should at the very least be made clear that the entity is expected only to make reasonable, but not exhaustive, efforts to identify such assets.

### ***Other matters***

If it is decided at a later stage in this project that the impairment-only approach to goodwill should be retained, then it would be appropriate, in our view, to extend to IFRS preparers the relief currently accorded to US preparers by Topic 350 which 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 before proceeding to a full impairment test. This would help ensure that IFRS preparers do not suffer a burden compared with their competitors in the USA.

Finally, although we recognise that IFRS 3 is a standard that is highly consistent with the equivalent US standard, we think that the topic of goodwill amortisation is so important to the rest of the world that EFRAG and the IASB should not be deterred from making changes in this area by the constraints of an agenda of convergence. Nevertheless, we consider that the arguments advanced for the reintroduction of goodwill amortisation should be considered by other standard setters, with the aim of avoiding divergence.

We remain at your disposal should you wish to discuss this subject further.

Yours sincerely,

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Deputy Director General