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EFRAG

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SHOULD GOODWILL STILL NOT BE AMORTISED?

ACCOUNTING AND DISCLOSURE FOR GOODWILL

Representing preparers' point of view, the Swedish Enterprise Accounting Group (SEAG) welcomes the initiative by the Research Group to carry out research in the very important area of goodwill and other intangible assets with indefinite useful lives. Earlier this year we responded to IASB's Post-implementation Review of IFRS 3 and also had some informal discussions with EFRAG staff members.

One message in our answer to PiR IFRS 3 was that we strongly believe that all intangible assets, including goodwill, should be amortised. Choosing useful lives will of course be difficult but will at least show some consumption of the assets. This was also conveyed to EFRAG in 2012 when responding to their questionnaire on goodwill impairment and amortisation. Another strong message to IASB was that we seriously doubt that it is possible to create impairment tests that can provide the needed information to be able to measure intangible assets and goodwill with enough accuracy.

We believe that the Research Group has carried out a very good analysis and have raised a number of important questions. In summary we have the following thoughts:

- We firmly believe that all intangible assets, including goodwill, should be amortised.
- IFRS should indicate a maximum amortisation period but allow entities to elect the appropriate periods.
- Amortisation should lead to simplifications of impairment tests and reduction of disclosures.

This is further elaborated in our answers to the Research Group's questions in the Appendix.

We are pleased to be at your service in case further clarification to our comments will be needed.

Yours sincerely,

CONFEDERATION OF SWEDISH ENTERPRISE

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The Swedish Enterprise Accounting Group (SEAG) represents more than 40 international industrial and commercial groups, most of them listed. The largest SEAG companies are active through sales or production in more than 100 countries.

Appendix

Question 1

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

We believe that the Research Group has made a very good analysis and fully agree to the conclusions that goodwill should be recognised as an asset and should be amortised.

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;

One important reason for amortisation is the replacement of the acquired goodwill by internally generated goodwill and it is hard for us to envision that there should be methods to capture this replacement with any accuracy.

(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

This is another important reason for amortisation of goodwill (and all other intangible assets) where we fully agree to the lack of reliability in the current impairment models, although a lot of resources are put into the processes.

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

From our discussions with users, we believe that their confidence in the reporting of intangible assets originating from business combinations in many cases is rather low. This means that the resources put into impairment tests must be reduced which should be possible if intangible assets are amortised. We are also concerned about the increased proportion of goodwill in relation to total assets. A recent study, made by Björn Gauffin and Sven-Arne Nilsson, shows that the share of goodwill in relation to total assets in 37 companies on Nasdaq OMX Nordic Stockholms's Large cap list has grown from 4.7% to 8.9% over the period 2006 to 2013. Mandatory amortisation of goodwill would, in our opinion, limit this "growth of goodwill".

Question 2

Assuming that there was a requirement to amortise goodwill, do you think that the IASB should:
(a) indicate what the amortisation period should be?

No, we believe that there are considerable differences in many cases which means that uniform amortisation periods can't be used.

(b) indicate a maximum amortisation period?

Yes, we believe an indicative maximum period should be stated with requirements for explanations if longer periods are chosen.

(c) provide guidance on how entities should assess the amortisation period (for instance, by referring to the expected payback period or the useful life of the primary asset)?

Yes, guidance if of course important in this critical area but should still be principle based and not to specific.

(d) allow entities to elect the amortisation period that they consider appropriate?

Yes, however within the maximum period allowed and in line with the guidance given.

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.

In our comment letter to the IASB regarding the PiR IFRS 3 we stated that the current impairment models lead to a lot of work without really solving problems with finding cash flow streams and internally generated goodwill etc. and the whole concept is perceived to be rather poorly understood by the users. One important challenge we face as preparers is to define cash flow and CGU when the business acquired develops, time is passing and particularly when restructuring is done within the group. In addition we have the problem of internally generated goodwill and also the fact that the goodwill is a residual based on fair values that are often not entity-specific (the fair values of acquired assets and liabilities are the “market values”). We therefore strongly recommended that all intangible assets, including goodwill, should be amortised.

We seriously doubt that it is possible to create impairment tests that can provide the needed information to be able to measure intangible assets and goodwill with enough accuracy. A review of the guidance in IAS 36 must be accompanied by a review of the current fair value measurements of acquired assets and liabilities and the resulting residual goodwill. In our view good impairment models are of course vital for financial reporting but if all intangible assets including goodwill are amortised, the importance of impairment tests should be less critical.

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 DP contains a good and interesting discussion on review of disclosures and we find a number of the ideas and suggestions worth considering. However, without a thorough review of the current fair value measurements of acquired assets and liabilities and the resulting residual goodwill we believe that the information will still be poorly understood by the users.

Amortisation of all intangible assets including goodwill should enable fewer disclosures. We get the impression that the risk is that the workload for the disclosures would increase following the intentions in the DP leading to an even more negative cost/benefit assessment.

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 the 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?

We believe that the same requirements should be extended to other intangible assets, i.e. prescribe similar treatment with a maximum amortisation period and principles for determining it.

In our comment letter regarding PiR IFRS 3 we stated that separate recognition of other intangible assets can't be avoided if a complete picture of a business combination shall be reported. It contributes to lower goodwill amounts, which we believe is essential since goodwill is a residual. However, we also pointed out that the recognised amounts of those intangible assets should be entity-specific and also, to really mirror the entities' investment decisions, include e.g. assembled workforces which we believe can be one vital component of certain business combinations.