(Translation for reference)

To: ASBJ/EFRAG/OIC

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Keidanren (Japan Business Federation)
Committee on Corporate Accounting
Sub-Committee on Corporate Accounting

Comments on Discussion Paper

Should Goodwill Still Not Be Amortised? - Accounting and Disclosure for Goodwill

Let us first appreciate the development of the Discussion Paper (DP) which suggests that the "amortisation of goodwill should be reintroduced", given that discussion on whether goodwill should be amortised is of a major concern to companies and market participants in Japan.

We at Keidanren previously provided our comment to the IASB's *Agenda Consultation 2011* that IFRS should be improved in a direction toward amortisation of goodwill. In addition, the Exposure Draft of "Japan's Modified International Standards (JMIS)" developed by the Accounting Standards Board of Japan (ASBJ) reflects the view that IFRS should be modified to require amortisation of goodwill. Introduction of amortisation of goodwill would enable appropriate matching between income and expenses subsequent to business combinations and provide discipline to entity's management so as to prevent imprudent M&As. Furthermore, a requirement to amortise goodwill would achieve a cost-benefit balance.

As with the amortisation of goodwill, we strongly hope that accounting standards should be converged internationally. Whether or not to amortise goodwill is a key issue that directly leads to the global competitiveness of entities, and thus the IASB and the FASB should avoid reaching different conclusions on this issue in their future discussions. Therefore, we believe that extensive discussions should be conducted, not just by the IASB, but together with the FASB and other relevant standard setters, in order to unify the accounting treatment as the global standards. We wish eagerly that global convergence will be ultimately achieved on the basis of a goodwill amortisation model, and we are committed to make contributions to the discussion.

Although we agree with the suggestion to reintroduce amortisation of goodwill, we

disagree with the suggestions regarding impairment testing and disclosures intended to make impairment testing more rigorous and to enhance disclosure requirements. Specifically, although the DP consists of three key elements, namely “reintroduction of amortisation of goodwill”, “improvements to impairment testing” and “improvements to disclosures”, these suggestions do not seem to be founded in the same grounds, because suggestions of “improvements to impairment testing” and “improvements to disclosures” seem to be based on the assumption that goodwill is not amortised. We believe that the impairment testing and disclosures should be simplified, if goodwill were to be amortised. Accordingly, in parallel with the discussions on amortisation of goodwill, the discussion regarding how to simplify impairment testing and disclosure requirements should be explored further in the future.

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.

(Comments)

We agree with the suggestion in the DP to reintroduce systematic amortisation of goodwill. As described below, in our view, the “amortisation plus impairment model” should be reintroduced, because it is preferable both from theoretical and cost-benefit perspectives.

In particular, we believe that the reason set out in (a) in the DP is the most fundamental. Introduction of amortisation of goodwill would enable appropriate matching between the increase in income as a result of the business combination and the corresponding expense that represents part of consideration paid. Amortisation of goodwill is also consistent with the view that perceives the excess recovery over the

cost of investments as income for an entity. In addition, because goodwill is replaced with internally generated goodwill over time, not recognising the decrease in value of goodwill through non-amortisation of goodwill (which we believe is a wasting asset) would, in effect, give rise to recognition of internally generated goodwill. We believe that systematic amortisation of goodwill would effectively prevent recognition of internally generated goodwill that may occur under the non-amortisation approach.

With regard to the reason set out in (b) in the DP, we think the conclusion in the DP that the impairment-only model is not sufficiently reliable is not necessarily appropriate, referring to the effect that the "amortisation plus impairment model" suggested in the DP also requires impairment testing and uses various assumptions and estimates as the impairment-only model does. At the same time, however, we believe that the "amortisation plus impairment model" would better ensures more objective and reliable accounting figures than the "impairment only model", because introduction of systematic amortisation of goodwill would lower the risk of impairment losses and reduce the risk of arbitrary estimates in impairment testing. Although some argue that an estimate of the amortisation period is arbitrary, we believe that amortising goodwill over a period determined based on a payback period would enable an entity to provide information that would better reflect the economic realities, because it would enable appropriate matching between income and expenses in that period, and would better reflect the management's intention for acquisitions in the financial statement.

We also agree with the reason set out in (c) in the DP. In our view, the "amortisation plus impairment model" has greater benefits than the "impairment-only model", because it is more appropriate from the accounting theoretical perspective and provides more objective and reliable figures, as described above. In addition, while annual impairment testing under the "impairment-only model" involves significant costs, systematic amortisation under the "amortisation plus impairment model" would reduce the risks of recognising impairment loss and is also practical in terms of costs. Combined altogether, we believe that the "amortisation plus impairment model" would achieve a better cost-benefit balance than the "impairment only model".

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?
(b) indicate a maximum amortisation period?
(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)?
(d) allow entities to elect the amortisation period that they consider appropriate?

(Comments)

We agree, in principle, with the suggestions set out in (a) through (d) in the DP. However, we note the following points.

With regard to (b), we believe that it would be appropriate to establish the maximum amortisation period between 10 and 20 years. However, a longer period should be allowed when the maximum period as a rebuttable assumption is reasonably rebutted, because different business acquisitions have different characteristics.

With regard to (c), whereas guidance as described in paragraph 84(c) of the DP may be useful, such guidance should be treated merely as a reference, because treating such guidance as a prescriptive rule might lead to superficial judgment in practice. In addition, we note that the DP states that "an entity would *normally* consider the following factors in determining the amortisation period". We believe that the word 'normally' in the statement in the DP should be deleted, because this phrase might result in such guidance being treated as a checklist.

With regard to (d), we believe that entities should be allowed to elect an amortisation period that suits the realities, because management is in the best position to judge the realities of the entity.

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.

(Comments)

We disagree with the proposed guidance in relation to (a) through (d), because they are based on the assumption that goodwill is not amortised. If any improvements and/or additions to guidance were to be made, it should aim at simplifying impairment testing under the assumption that amortisation of goodwill should be reintroduced. If amortisation of goodwill were to be reintroduced, impairment testing should be limited to cases where there is an indication of impairment, instead of requiring annual impairment testing, given that consumption of goodwill would be reflected in subsequent measurement. When amortisation of goodwill is introduced, delay of recognition of impairment would not arise even if impairment testing is limited to cases where there is an indication. We believe that this approach is preferable also from the cost-benefit perspective.

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.

(Comments)

We strongly disagree with the suggested disclosure requirements for (a) through (c) in the DP. Disclosure requirements in IAS 36 and IFRS 3 are already extensive, and thus such additional disclosure requirements would not bring additional benefits that justify costs. In addition, we disagree with the suggestion of enhancing the disclosure requirements immediately, considering the consistency with the discussions on Disclosure Framework currently undertaken by the IASB If goodwill (which we believe is a wasting asset) is not amortised, impairment losses will surely arise in the future as a theoretical consequence and thus rigorous impairment testing involving a

number of practical challenges would be necessary. We believe that it is inappropriate to attempt to address this issue through enhanced disclosure requirements in the first place. This issue should rather be addressed by reconsideration of the accounting treatment (that is the reintroduction of amortisation of goodwill). If amortisation of goodwill were to be reintroduced, simplification of disclosures should be explored.

<(a) Inputs to the discount rate, paragraphs 140 to 144>

We disagree with the suggestion in the DP that the discount rate should be disclosed by the periods covered, or by the cash generating units for the time series and the reason for the changes, as well as liquidly premium incorporated. While such disclosures can become voluminous because an entity may have many cash generating units, it is entirely unclear how users can utilise such detailed data in their investment decisions.

<(b) Analysis of variances, paragraphs 146 to149>

We disagree with the suggestion in the DP to require disclosure of variances between forecasts and actual results. The DP suggests introducing the disclosure requirement on a uniform basis of such forecast information, which would present the management judgment and management view as to the entity’s business environments. In our view, such disclosures would lead to excessive leakage of internal information and would ruin the corporate value. In addition, it is difficult to identify the forecast information and the corresponding actual figures to analyse. For example, when the synergy effect composes goodwill as an excess earning power, it is not easy to extract only the results arising from the synergy to keep track of and disclose them as verifiable information. We believe that information in the notes of financial statements should be provided to support objectivity of accounting figures; and the “disclosure of variance” suggested in the DP is a significant departure from this concept.

<(c) Expected timing of impairment, paragraphs 156 to 158>

We disagree with the suggestion in the DP to require disclosure for the time period over which an entity expects to consume the excess earning power. Such quantitative disclosure based on the entity’s expectation is impossible for an entity to provide in fulfilling its accountability through accounting information, and would impose significant difficulties in auditing. In addition, it would lead to excessive leakage of internal information and would ruin the corporate value.

<(c) Acquisition characteristics that point to future impairment, paragraphs 159

to161>

We strongly disagree with the suggestion in the DP to require disclosure of premiums paid in excess of market price. Consideration paid for a business combination is determined through negotiations between the parties involved, and it would best represent the value of the acquired business. Aside from such consideration, it is impossible to determine objective market values. In addition, such disclosures may have significant harmful effects on the business such as litigations. Proposals for disclosure requirements should not be made recklessly without due consideration of the significant costs and risks of entities required to make the disclosure.

<(c) Reconciliation of total goodwill, paragraphs 162>

We strongly disagree with the suggestion in the DP to require disclosures regarding full reconciliation of the goodwill allocated to cash generating units. While disclosures of an entity's internal organisational structure may be severely detrimental to the entity, we do not believe that the benefits to users would be sufficiently large compared with the "disclosure of cash generating units with a significant amount of goodwill" that is already required under the current requirements.

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?

(Comments)

We believe that, if goodwill were to be amortised as part of the cost of the acquisition to match with the income over the periods for which the acquisition will have effect, it is inappropriate to separately recognise intangible assets that are not within the purpose of the business combination from goodwill. In line with this thinking, we believe that all intangible assets should have definite useful lives, in principle. Yet, it should also be noted that the value of some intangible assets, such as telephone subscription rights and leasehold with no specified terms, do not diminish over time.