Norsk RegnskapsStiftelse

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International Accounting Standards Board
Email: commentletters@ifrs.org

Cc: EFRAG

Dear Sir/Madam

Discussion paper (DP) 2020/1: Business combinations – Disclosures, Goodwill and Impairment

Norsk Regnskapsstiftelse (the Norwegian Accounting Standards Board, NASB) welcomes the opportunity to submit our views on DP 2020/1: Business combinations – Disclosures, Goodwill and Impairment.

In general, we welcome the project and support many of the DP's proposals. We believe the proposal could improve the information provided for acquisitions without undue costs on preparers. We believe that IASB has found the right level of information to be disclosed.

We support the objective of improving the financial reporting for use in monitoring the stewardship of management, one of the two key objectives of financial statements according to the framework. In order to measure stewardship, management should be held accountable for the resources they spend on acquisitions. The DP is silent on the fact that when shares are used as consideration, management make their decision based on the value of those shares on the date of agreement, whereas goodwill is measured based on the value when control passes. This is often at a date significantly later, and which may be considerably higher. Often the change in price may have little or no connection to the acquisition itself. If the Board wants to improve the accounting for stewardship purposes, this inconsistency should be remedied.

We have mixed views within NASB but lean to a view that goodwill is a wasting asset for which the current model doesn't fully reflect its consumption. We therefore challenge the Board's preliminary view that it should not reintroduce amortisation of goodwill. However, if the impairment only model is continued, we ask the Board to assess whether certain components currently included in goodwill, e.g. "technical" goodwill connected to fair value adjustments of deferred tax liabilities in acquisition, could be amortised separately. Again, if not, it should be made clearer that a component of goodwill arising due to nominal measurement of a deferred tax liability of a particular tax jurisdiction will have to be tested at the level of that entity. In general, we support the proposed modifications to the impairment model.

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We have noted that FASB's project related to ASC 350 *Intangibles – Goodwill and Other* deals with a number of the same issues. We strongly urge the IASB to ensure that two different treatments for goodwill do not develop in the global capital market.

We are available to further discuss our comments. Please do not hesitate to contact the undersigned.

Yours faithfully,

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SECTION 1 INTRODUCTION

Question 1

Paragraph 1.7 summarises the objective of the Board's research project. Paragraph IN9 summarises the Board's preliminary views. Paragraphs IN50–IN53 explain that these preliminary views are a package and those paragraphs identify some of the links between the individual preliminary views.

The Board has concluded that this package of preliminary views would, if implemented, meet the objective of the project. Companies would be required to provide investors with more useful information about the businesses those companies acquire. The aim is to help investors to assess performance and more effectively hold management to account for its decisions to acquire those businesses. The Board is of the view that the benefits of providing that information would exceed the costs of providing it.

(a) Do you agree with the Board's conclusion? Why or why not? If not, what package of decisions would you propose and how would that package meet the project's objective?

(b) Do any of your answers depend on answers to other questions? For example, does your answer on relief from a mandatory quantitative impairment test for goodwill depend on whether the Board reintroduces amortisation of goodwill?
Which of your answers depend on other answers and why?

We agree with the overall objective to provide investors with more useful information about acquisitions. We believe that the objective may be fulfilled by the proposed disclosures.

The disclosures proposed for an acquisition would result in information that is relevant and at a reasonable cost. We welcome that the information required is not rigid or pre-defined, but reflects the acquirer's situation, management's monitoring of the acquisition and changes in metrics over time, as there are major differences in for example the complexity, size and industries affecting what is deemed useful information about an acquisition.

SECTION 2 IMPROVING DISCLOSURES ABOUT ACQUISITIONS

Question 2

Paragraphs 2.4–2.44 discuss the Board's preliminary view that it should add new disclosure requirements about the subsequent performance of an acquisition.

(a) Do you think those disclosure requirements would resolve the issue identified in paragraph 2.4—investors' need for better information on the subsequent performance of an acquisition? Why or why not?

(b) Do you agree with the disclosure proposals set out in (i)–(vi) below? Why or why not?

(i) A company should be required to disclose information about the strategic rationale and management's (the chief operating decision maker's (CODM's)) objectives for an acquisition as at the acquisition date (see paragraphs 2.8–2.12). Paragraph 7 of IFRS 8 *Operating Segments* discusses the term 'chief operating decision maker'.

(ii) A company should be required to disclose information about whether it is meeting those objectives. That information should be based on how management (CODM) monitors and measures whether the acquisition is meeting its objectives (see paragraphs 2.13–2.40), rather than on metrics prescribed by the Board.

(iii) If management (CODM) does not monitor an acquisition, the company should be required to disclose that fact and explain why it does not do so. The Board should not require a company to disclose any metrics in such cases (see paragraphs 2.19–2.20).

(iv) A company should be required to disclose the information in (ii) for as long as its management (CODM) continues to monitor the acquisition to see whether it is meeting its objectives (see paragraphs 2.41–2.44).

(v) If management (CODM) stops monitoring whether those objectives are being met before the end of the second full year after the year of acquisition, the company should be required to disclose that fact and the reasons why it has done so (see paragraphs 2.41–2.44).

(vi) If management (CODM) changes the metrics it uses to monitor whether the objectives of the acquisition are being met, the company should be required to disclose the new metrics and the reasons for the change (see paragraph 2.21)

(c) Do you agree that the information provided should be based on the information and the acquisitions a company's CODM reviews (see paragraphs 2.33–2.40)? Why or why not? Are you concerned that companies may not provide material information about acquisitions to investors if their disclosures are based on what the CODM reviews? Are you concerned that the volume of disclosures would be onerous if companies' disclosures are not based on the acquisitions the CODM reviews?

(d) Could concerns about commercial sensitivity (see paragraphs 2.27–2.28) inhibit companies from disclosing information about management's (CODM's) objectives for an acquisition and about the metrics used to monitor whether those objectives are being met? Why or why not? Could commercial sensitivity be a valid reason for companies not to disclose some of that information when investors need it? Why or why not?

(e) Paragraphs 2.29–2.32 explain the Board's view that the information setting out management's (CODM's) objectives for the acquisition and the metrics used to monitor progress in meeting those objectives is not forward-looking information. Instead, the Board considers the information would reflect management's (CODM's) targets at the time of the acquisition. Are there any constraints in your jurisdiction that could affect a company's ability to disclose this information? What are those constraints and what effect could they have?

We agree that the disclosure requirements will give better information about acquisitions, focusing on management strategies and the rationale for the acquisition. In practice this is also communicated when the acquisition is published in the market through press releases and other means of communication. Nevertheless, we support that business rationale for significant acquisitions should be disclosed in the financial statements to ensure the completeness of relevant information in the financial reporting.

We agree with the proposal in (b)(i) to replace the current requirements to disclose "the primary reasons for an acquisition" with a requirement to disclose information about the strategic rationale and objectives for an acquisition at the acquisition date.

We also support the proposal in (b)(ii) that how management (CODM) monitors and measures the acquisition is at an appropriate level of details. The metrics disclosed will give investors relevant information about how management monitors and follows up an acquisition and about how well a company is managed. For quantitative disclosure requirements, the Board should be clear that only metrics that can be measured (and audited) with sufficient reliability should be within the scope for quantitative disclosures. This would limit the disclosures with regard to metrics related to e.g. future cost savings or improvements for which limited reliable audit evidence is available.

Even though we support the inclusion of the above disclosure requirements, we notice that two different growth strategies (organic growth versus growth via acquisitions) will lead to distinct differences in the level of information provided in the financial statements. For a company with a mixed growth strategy, users will get significantly more information about acquired businesses than about businesses developed internally, even though the resources used may be of similar magnitude. We acknowledge that organic and acquired growth is different, but we are not convinced that such asymmetry is in the interest of the users of the financial statements.

We support proposal b(iii) as we see value in informing investors about whether an acquisition is followed up directly by the CODM or by a lower level of management either as a stand-alone entity or through integration with existing business. We do however ask the Board to be careful with regards to the use of negative statements in the disclosure as this can take attention away from the information management has considered useful and included in the disclosures

We support the proposal in (b)(v). Since the acquired business will change over time and often will be integrated in the total business, we find the two-year period appropriate.

Based on the fast-changing environment, integration of the acquired company into the existing business and the fact that all acquisitions are different, we support the requirement in (b)(vi) to disclose any change in the metrics used and the reason for the changes.

Regarding the question about commercial sensitivities in (d), we generally think the information can be disclosed without affecting the commercial situation. We have also listened to the producers with regards to this question. Based on their experiences it is often possible to give relevant information to the market without harming the company. But it depends on the level of details and timing. Information about how the company will achieve the synergies, information about price expectations, specification of cost reductions and information affecting employees will often be sensitive after an acquisition.

Question 3

Paragraphs 2.53–2.60 explain the Board's preliminary view that it should develop, in addition to proposed new disclosure requirements, proposals to add disclosure objectives to provide information to help investors to understand:

• the benefits that a company's management expected from an acquisition when agreeing the price to acquire a business; and
• the extent to which an acquisition is meeting management's (CODM's) objectives for the acquisition.

Do you agree with the Board's preliminary view? Why or why not?

We support the Board's preliminary view to describe the disclosure objectives in the standard, and that these should focus on benefits the company's management expects from the acquisition and subsequent measurement of whether those expectations were fulfilled. The proposed disclosure objectives related to the expected benefits from the acquisition place strong stewardship on management and will strengthen corporate governance.

Question 4

Paragraphs 2.62–2.68 and paragraphs 2.69–2.71 explain the Board's preliminary view that it should develop proposals:

• to require a company to disclose:
○ a description of the synergies expected from combining the operations of the acquired business with the company's business;
○ when the synergies are expected to be realised;
○ the estimated amount or range of amounts of the synergies; and
○ the expected cost or range of costs to achieve those synergies; and

• to specify that liabilities arising from financing activities and defined benefit pension liabilities are major classes of liabilities.

Do you agree with the Board's preliminary view? Why or why not?

We agree that the Board should develop proposals that require companies to disclose expected synergies and when the synergies are expected to be realized. However, we do not believe the disclosure should always require detailed requirements about estimated amount or range of amounts of the synergies, and the expected cost or range of costs to achieve those synergies. There should be a reliability threshold, as included in other standards, before quantitative information is mandated. Mandating such a disclosure in all instances seem to conflict with the overall direction of the DP, which is to report on metrics that are reported to the CODM. The disclosure requirements should be useful and flexible, and based on the company's governance and monitoring of the acquisitions. Further, as synergies are not well defined, there are complexities around the audit of such concrete measures.

We oppose requirements for companies to separate liabilities arising from financing activities from defined pension liabilities. In our jurisdiction, defined benefit plans are being phased out, and liabilities are normally settled as part of the acquisition. IAS 7.44B already requires disclosure of changes in liabilities from financing activities arising from obtaining control of a business and IAS 19.141(h) requires the disclosure of the effect of business combinations as part of the reconciliation of the net defined benefit liability (asset). We do not support duplicating those disclosure requirements.

Question 5

IFRS 3 *Business Combinations* requires companies to provide, in the year of acquisition, pro forma information that shows the revenue and profit or loss of the combined business for the current reporting period as though the acquisition date had been at the beginning of the annual reporting period.

Paragraphs 2.82–2.87 explain the Board's preliminary view that it should retain the requirement for companies to prepare this pro forma information.

(a) Do you agree with the Board's preliminary view? Why or why not?

(b) Should the Board develop guidance for companies on how to prepare the pro forma information? Why or why not? If not, should the Board require companies to disclose how they prepared the pro forma information? Why or why not?

IFRS 3 also requires companies to disclose the revenue and profit or loss of the acquired business after the acquisition date, for each acquisition that occurred during the reporting period.

Paragraphs 2.78–2.81 explain the Board's preliminary view that it should develop proposals:

• to replace the term 'profit or loss' with the term 'operating profit before acquisition-related transaction and integration costs' for both the pro forma information and information about the acquired business after the acquisition date.
Operating profit or loss would be defined as in the Exposure Draft *General Presentation and Disclosures*.
• to add a requirement that companies should disclose the cash flows from operating activities of the acquired business after the acquisition date, and of the combined business on a pro forma basis for the current reporting period.

(c) Do you agree with the Board's preliminary view? Why or why not?

We support the Board's preliminary view to retain the requirement for companies to prepare the pro forma information for the combined business as though the acquisition had taken place at the beginning of the annual reporting period.

It should not be a priority of the Board to develop guidance on how to prepare the pro forma information. We believe such guidance could be more misleading than clarifying, and that it will be challenging to address specificities of all industries. We believe it is appropriate for entities to establish relevant accounting policies on how to prepare the pro forma information and disclose those in the financial statements taking into consideration the views of the regulators.

We support the proposal to replace the term "profit or loss" with the term "operating profit" (as would be defined in the Exposure Draft General Presentation and Disclosures) for both the pro forma information and information about the acquired business after the acquisition date.

SECTION 3 GOODWILL AND AMORTISATION

Question 6

As discussed in paragraphs 3.2–3.52, the Board investigated whether it is feasible to make the impairment test for cash-generating units containing goodwill significantly more effective at recognising impairment losses on goodwill on a timely basis than the impairment test set out in IAS 36 *Impairment of Assets*. The Board's preliminary view is that this is not feasible.

(a) Do you agree that it is not feasible to design an impairment test that is significantly more effective at the timely recognition of impairment losses on goodwill at a reasonable cost? Why or why not?

(b) If you do not agree, how should the Board change the impairment test? How would those changes make the test significantly more effective? What cost would be required to implement those changes?

(c) Paragraph 3.20 discusses two reasons for the concerns that impairment losses on goodwill are not recognised on a timely basis: estimates that are too optimistic; and shielding. In your view, are these the main reasons for those concerns? Are there other main reasons for those concerns?

(d) Should the Board consider any other aspects of IAS 36 in this project as a result of concerns raised in the Post-implementation Review (PIR) of IFRS 3?

We appreciate the thorough work and assessment done by the Board in investigation if it is feasible to make the impairment test for cash-generating units containing goodwill more effective, including the discussions of shielding effects and other complex methods. We believe it is challenging to find more effective methods for the impairment test and support the Board's overall preliminary view.

We agree that management's optimism and shielding are the main sources for delayed impairment. As for shielding, this is an inevitable effect of combining and integrating businesses, however it could be clarified that components of goodwill that relates to a particular legal entity, such as deferred-tax-goodwill ("Technical goodwill") and employees should be kept at that entity level for impairment testing purposes.

The Board recognises in 3.105-106 that goodwill comprises various components but rejected to develop an approach where some components may be amortised or written off immediately. We believe this conclusion should be revisited. We suggest introducing a narrow scope exemption for components of goodwill related to nominal measurement of deferred tax liabilities which may amount to large amounts and give these a separate treatment. Amortisation of such components over the expected reversal period of those temporary differences is one reasonable approach. However, if amortisation of such a component is deemed to create too much complexity, we recommend that such a component should be tested for impairment at the level of the tax entity that creates the component, and not at any higher level. IAS 36 already requires goodwill to be allocated to the units that benefit from the synergies of the combination, and IAS 21 requires goodwill to be retranslated at the level of the different currencies, so guidance to require testing at the tax entity level would be aligned with the current concepts.

Question 7

Paragraphs 3.86–3.94 summarise the reasons for the Board's preliminary view that it should not reintroduce amortisation of goodwill and instead should retain the impairment-only model for the subsequent accounting for goodwill.

(a) Do you agree that the Board should not reintroduce amortisation of goodwill? Why or why not? (If the Board were to reintroduce amortisation, companies would still need to test whether goodwill is impaired.)

(b) Has your view on amortisation of goodwill changed since 2004? What new evidence or arguments have emerged since 2004 to make you change your view, or to confirm the view you already had?

(c) Would reintroducing amortisation resolve the main reasons for the concerns that companies do not recognise impairment losses on goodwill on a timely basis (see Question 6(c))? Why or why not?

(d) Do you view acquired goodwill as distinct from goodwill subsequently generated internally in the same cash-generating units? Why or why not?

(e) If amortisation were to be reintroduced, do you think companies would adjust or create new management performance measures to add back the amortization expense? (Management performance measures are defined in the Exposure Draft
General Presentation and Disclosures.) Why or why not? Under the impairment-only model, are companies adding back impairment losses in their management performance measures? Why or why not?

(f) If you favour reintroducing amortisation of goodwill, how should the useful life of goodwill and its amortisation pattern be determined? In your view how would this contribute to making the information more useful to investors?

There is no firm consensus in NASB on whether to keep the impairment only model or reintroduce amortisation of goodwill. The majority views goodwill as a wasting asset for which the current model doesn't fully reflect its consumption and hence support a reintroduction of amortisation of goodwill.

The amortisation pattern to be applied should be based on a judgment by the companies and one could also assess whether goodwill can be split into different components with different useful lives. Even though goodwill is a residual, the companies will often be able to assess how long they will benefit from the goodwill. As for other items in the financial statements, the accounting policy, if material, should be disclosed.

If amortisation of goodwill is reintroduced, we have no firm indication whether this amortisation will be adjusted out in management performance measures. Although it is rather arbitrary, we assume that the amortisation expense will be considered as a periodic expense connected to a wasting assets (goodwill), and therefore not adjusted out to the same extent as the current "too much too late" impairment charge.

If an impairment only model is continued, we are of the opinion that certain items currently included in goodwill should be separated out of goodwill and allocated to profit and loss when appropriate. For instance, technical goodwill related to the nominal deferred tax liabilities incurred in acquisitions should be separated out of goodwill and allocated to profit or loss in the same period as the tax is settled. If such an approach is not feasible, a more prescriptive guidance on how such a component of goodwill should be tested for impairment is warranted. It should be made clear that a component of goodwill arising due to nominal measurement of a deferred tax liability of a particular tax jurisdiction will have to be tested at the level of that entity.

Question 8

Paragraphs 3.107–3.114 explain the Board's preliminary view that it should develop a proposal to require companies to present on their balance sheets the amount of total equity excluding goodwill. The Board would be likely to require companies to present this amount as a free-standing item, not as a subtotal within the structure of the balance sheet (see the Appendix to this Discussion Paper).

(a) Should the Board develop such a proposal? Why or why not?

(b) Do you have any comments on how a company should present such an amount?

We oppose the proposal to present Total equity excluding goodwill. We believe this subtotal can easily be calculated by the users of the financial statements, and the information is readily available. If the Board has any rationale for why goodwill should be treated differently from other assets, this issue needs to be discussed further.

SECTION 4 SIMPLIFYING THE IMPAIRMENT TEST

Question 9

Paragraphs 4.32–4.34 summarise the Board's preliminary view that it should develop proposals to remove the requirement to perform a quantitative impairment test every year. A quantitative impairment test would not be required unless there is an indication of impairment. The same proposal would also be developed for intangible assets with indefinite useful lives and intangible assets not yet available for use.

(a) Should the Board develop such proposals? Why or why not?

(b) Would such proposals reduce costs significantly (see paragraphs 4.14–4.21)? If so, please provide examples of the nature and extent of any cost reduction. If the proposals would not reduce costs significantly, please explain why not.

(c) In your view, would the proposals make the impairment test significantly less robust (see paragraphs 4.22–4.23)? Why or why not?

There were mixed views within the NASB on this issue but the majority, supported by the local outreach event, support the Board's view that an annual test is not required but should be based on whether an impairment indicator exists or not, similar as for other types of asset in accordance with IAS 36.

Question 10

The Board's preliminary view is that it should develop proposals:
• to remove the restriction in IAS 36 that prohibits companies from including some cash flows in estimating value in use—cash flows arising from a future uncommitted restructuring, or from improving or enhancing the asset's performance (see paragraphs 4.35–4.42); and
• to allow companies to use post-tax cash flows and post-tax discount rates in estimating value in use (see paragraphs 4.46–4.52).

The Board expects that these changes would reduce the cost and complexity of impairment tests and provide more useful and understandable information.
(a) Should the Board develop such proposals? Why or why not?
(b) Should the Board propose requiring discipline, in addition to the discipline already required by IAS 36, in estimating the cash flows that are the subject of this question? Why or why not? If so, please describe how this should be done and state whether this should apply to all cash flows included in estimates of value in use, and why.

We support the proposal also to use post-tax cashflows and post-tax discount rates in estimating value in use. We have experiences that this already has been a practical approach in determining the cash flows used to calculate value in use.

We support the Board in removing the restriction in IAS 36 that prohibits companies from including cash flows in estimating value-in-use arising from a future planned, but uncommitted, restructuring, or from planned improvement or enhancement of the asset's performance. Uncertain estimates are not unique for impairment assessments and should be treated in the same way as for other estimates.

Question 11

Paragraph 4.56 summarises the Board's preliminary view that it should not further simplify the impairment test.

(a) Should the Board develop any of the simplifications summarised in paragraph 4.55? If so, which simplifications and why? If not, why not?

(c) Can you suggest other ways of reducing the cost and complexity of performing the impairment test for goodwill, without making the information provided less useful to investors?

We support the Board in not pursing the above mentioned simplifications, but ask the Board to assess whether certain items currently included in goodwill, i.e. "technical" goodwill connected to deferred tax liabilities in acquisition could be separated out of goodwill, as the "use" of this goodwill is directly related to the settlement of the related deferred liability and should not be shielded by other assets.

We also propose that the Board assess whether the after-tax value-in-use may allow for the use of the actual tax cash flows due to unrecognized carry forward losses. Utilisation may be expected through the profit from the CGU, even though convincing evidence does not support recognition of a deferred tax assets. Such unrecognised carry forward losses acquired as part of an acquisition are included in goodwill recognised as part of the purchase price allocation, and the testing should reflect this fact.

SECTION 5 INTANGIBLE ASSETS

Question 12

Paragraphs 5.4–5.27 explain the Board's preliminary view that it should not develop a proposal to allow some intangible assets to be included in goodwill.

(a) Do you agree that the Board should not develop such a proposal? Why or why not?

(b) If you do not agree, which of the approaches discussed in paragraph 5.18 should the Board pursue, and why? Would such a change mean that investors would no longer receive useful information? Why or why not? How would this reduce complexity and reduce costs? Which costs would be reduced?

(d) Would your view change if amortisation of goodwill were to be reintroduced? Why or why not?

Based on the Board's arguments and discussions, we do agree with the Board's view not to develop a proposal to allow some intangible assets to be included in goodwill. Reducing the proportion of intangible assets recognised separately, would not respond to frequent calls to improve financial reporting by providing more information about intangible assets that are increasing in modern economies. We can't see that another conclusion will support the project objectives. This would be our view even if the Board reintroduces amortisation of goodwill.

SECTION 6 OTHER QUESTIONS

Question 13
IFRS 3 is converged in many respects with US generally accepted accounting principles (US GAAP). For example, in accordance with both IFRS 3 and US GAAP for public companies, companies do not amortise goodwill. Paragraphs 6.2–6.13 summarise an Invitation to Comment issued by the US Financial Accounting Standards Board (FASB). Do your answers to any of the questions in this Discussion Paper depend on whether the outcome is consistent with US GAAP as it exists today, or as it may be after the FASB's current work? If so, which answers would change and why?

We encourage the harmonisation of IFRS and US GAAP, and we strongly urge the IASB to avoid a situation where two different treatments of subsequent measurement of goodwill develops in the international capital market. Apart from goodwill amortisation, our views in this comment letter would not be influenced by the FASB's decisions as these are regarded as less fundamental.

Question 14
Do you have any other comments on the Board's preliminary views presented in this Discussion Paper? Should the Board consider any other topics in response to the PIR of IFRS 3?

We refer to our reply on question 11 with regards to separating out technical goodwill from goodwill into a separate intangible asset, or a separate component of goodwill, that may be subject to amortisation, or at least tested at the same level as the deferred tax.