SwissHoldings
Federation of Industrial
and Service Groups
in Switzerland

Nägeligasse 13
Postfach
CH-3001 Bern

+41 31 356 68 68
info@swissholdings.ch
www.swissholdings.ch

International Accounting Standards Board
Columbus Building
7 Westferry Circus
Canary Wharf
London E14 4HD
United Kingdom

Bern, 23 December 2020

Comment Letter on the Discussion Paper DP/2020/1"Business Combinations—Disclosures, Goodwill and Impairment"

Dear Madam, Dear Sir

SwissHoldings, the Swiss Federation of Industrial and Services Groups in Switzerland, represents 59 Swiss groups, including most of the country's major industrial and commercial enterprises. We very much welcome the opportunity to provide comments to this Discussion Paper (DP).

We recognise that there is legitimate interest from shareholders, investors and other users in these topics, and the DP is a useful starting point for these discussions. Our detailed answers to the questions in the DP are included below. However we would like to make the following specific remarks.

- We believe that additional disclosures on the objectives, targets and subsequent performance of business combinations are best addressed at a global regulatory level. We do not believe that such disclosures, in as far as they talk about governance and value-for-money considerations, belong in financial statements; and we question whether an accounting standards setter is the right body to be legislating on this. A useful analogy here is Executive Remuneration disclosures, where IAS 19 takes a relatively broad and high-level approach, and specific detailed requirements are left to the respective regulatory authorities.

- Having a global regulatory approach would ensure a level playing field, especially between IFRS preparers and their competitors who may be using US, Chinese or other accounting standards. To impose these at an IFRS level only would create a competitive disadvantage.

- We further believe that such disclosures, if needed, should be placed in the Management Discussion and Analysis and not in the Financial Statements.

- Such disclosures should only apply to public companies, and not to private companies and subsidiaries (in a similar manner to the application of IAS 33).

- Finally such disclosure requirements are an example of the kind of changes in IFRS that, in recent years, have led some small and medium-sized companies in Switzerland dropping IFRS in favour of the local Swiss-GAAP-FER standards. We believe this should be of concern to the IASB, as this may be illustrative of other jurisdictions where IFRS is not the only permitted financial accounting regime.

The minor improvements proposed in the goodwill impairment testing are welcome, but we would encourage the IASB not to invest too much time and energy trying to fix this in isolation. A comprehensive project to revisit the accounting and reporting of intangible assets in total is well overdue, to include goodwill and also internally generated intangibles; and we hope and support that the IASB can take this up at earliest opportunity.

Our response has been prepared in conjunction with our member companies. Please contact us if you require additional information.

Yours sincerely

SwissHoldings
Federation of Industrial and Service Groups in Switzerland

Dr Gabriel Rumo
Director

Denise Laufer
Member Executive Committee

cc SH Board

SwissHoldings

APPENDIX

QUESTIONS FOR RESPONDENTS

Question 1 - Introduction

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?

Answer to Question 1

a)

No. As set out below, we believe the proposals in the DP are poorly defined, and will not result in improved information for readers. Many transactions will be scoped out, and for those that are scoped in, much of the disclosure will be of limited use.

It seems to us that the proposals in this part of the DP are falling between two stools.

- We accept that there is a legitimate interest from shareholders and investors in very large transactions that use substantial amounts of the company's resources and represent a significant proportion of the company's market capitalisation. Acquisitions are particularly common example (not limited to Business

Combinations per IFRS 3), but the same considerations could extent to significant capital expenditure projects or research and development activities, or marketing initiatives, to name just three. Such governance, value-for-money, holding-management-to-account considerations are, in our view, better addressed as a global regulatory issue, and do not belong in financial statements.

We believe that the IASB should pursue a global approach with regulators on the need for governance-related disclosures for major acquisitions, or indeed other major transactions. This would need to be internationally aligned and not restricted to IFRS preparers.

- At the same time, it is clear that the accounting and disclosure for business combinations is not operating satisfactorily, notably for goodwill impairment testing. The solution here would seem to be to reduce or eliminate the work and disclosure on goodwill impairment testing, and rather expand the granularity of disclosure at the time of acquisition. We believe readers would be better able to assess subsequent performance if they had a clearer idea of what was acquired in the first place and then they can judge for themselves without the need for targets and performance assessment for that subset of deals that are captured by the DP proposals.

  At the same time there should be detailed review of IFRS 3 and IAS 36, with a view of increasing useful disclosures at the time of acquisition, and reducing non-useful disclosures on areas such as goodwill impairment.

b)

No. We believe the topic of goodwill amortisation vs impairment only is a red herring in this whole discussion. It is of (great) interest to many in the accounting profession and of little or no interest to anyone else. The fact that this consumes such a major part of the DP on this important topic, shows an accounting profession that is inward-looking and talking to itself, rather than listening to its customers. The IASB would be better advised to direct its resources to looking at intangible assets, holistically. We would certainly welcome leadership in this respect.

SwissHoldings

Question 2 - Improving disclosures about acquisitions

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?

Answer to Question 2

No.

Firstly the proposals are poorly defined. DP pp2.4 identifies "acquisitions" as being a strong concern of investors. However the DP does not anywhere define "acquisitions", it being missing from DP pp1.8, for example. Instead the proposals focus exclusively on Business Combinations as defined by IFRS 3 and ignore completely all other transactions that users would expect to be included in disclosures about acquisition activity. Specifically scoped out are:

- Purchases of companies that do not meet the definition of a business per IFRS 3, for example by applying the concentration test.
- Interests in Associates.
- Interests in Joint Arrangements.
- Purchases of specific assets, which for some targets may be the only significant asset in the company.
- Alliances, in-licensing and similar arrangements.
- Step-acquisitions and buy-outs of minorities, which are recorded directly to equity.

We would draw the IASB's attention to the operation of Mergers & Acquisitions (M&A) teams in most companies. These teams will be searching for targets with assets that be of interest to the company. The M&A team will generally be neutral about which of the specific arrangements listed above will be used, and in practice often move between different scenarios and may pursue one than one at the same time. For the company the choice relates to what works best, and of course what has the best price.

Therefore the assumptions that investors are only interested in the subset of M&A deals that meet the criteria of a Business Combination per IFRS 3, is a question that the IASB should address. We believe there is currently a very significant expectations gap between the volume of deals that some user-groups expect to be disclosed and the number that actually will.

As set out in our other answers below:

- We believe there are significant issues in the proposals in the DP as regards scoping in regards of the CODM.
- Acquisition are typically not “monitored” in the way that the DP imagines, and therefore many companies will not disclose anything in this respect as there would be nothing to disclose. We would expect that preparers would quickly coalesce around appropriate explanations as to why the acquisitions are not “monitored”, and there would be further boiler-plate disclosure such as currently exists for IAS 36 pp134 and IFRS 3 B64(e).

(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).

SwissHoldings

Answer to Question 2b

i) We agree that a more detailed qualitative discussion about the rationale and objectives for an acquisition would be useful to users. This is often anyway given in press releases and/or investor relations materials. Some of our members already replicate some or all of that information in the notes to the accounts. However we do not agree to providing targets or quantitative metrics for these objectives, as discussed below.

ii) We appreciate the IASB's approach to this, and agree that any disclosures should be based on internally already-existing information.

iii) All companies monitor acquisitions, however this is rarely done in the way that the DP imagines. Consequently this requirement would mostly lead to standard disclosures along the lines of DP 2.19.

iv) We believe this requirement will, in practice, result in such monitoring, if it exists, being "switched-off" sooner rather than later.

v) Again this would be lead to standard disclosure – we would rather expect that if a company goes to the time and trouble of setting up the monitoring imagined by the DP, then they will normally run this for more than one reporting period. The exception may be synergy reporting – in our experience of those who have tried it, it is usually abandoned after one or two quarterly cycles due to limited value and the internal time used to report it.

vi) We believe this is an open-ended requirement and should be much more tightly defined.

SwissHoldings

(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?

Answer to Question 2c

The proposal to limit information to that reviewed by the CODM is an interesting idea, and a welcome attempt to avoid disclosure overload. However we believe that this will be ineffective in practice and difficult to enforce, and will not achieve the objectives.

Firstly, this is situational and is based the company's current segment reporting and how it considers its CODM. For example in larger companies with multiple businesses, the CODM may be Corporate Executive Committee or Chief Executive Officer. But the review and monitoring, if it exists, may be done at a Divisional/Segment level.

Secondly, it is open to abuse. For example, a company not wishing to disclose such information has a simple remedy: move the review and monitoring, if it exists, to a level below the CODM.

We are therefore highly concerned that, absent some cap or limit, such as then CODM-proposal is trying to effect, then there will be a significant overload of disclosures. IFRS 3 is already disclosure-heavy as it is.

Should the IASB wish to further pursue these proposals, then we recommend some alternative limit to restrict these disclosures to the larger deals. One idea to explore could be where the deal price exceeds a certain percentage of the company's market capitalisation. This would provide a reasonable enforceable threshold that can be communicated to users simply.

(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?

Answer to Question 2d

Commercial sensitivity is a legitimate concern here.

Indeed it is already a legitimate concern for the existing disclosures required by goodwill impairment testing. Specifically our Investor Relations specialists have received questions relating to IAS 36 pp134(d) that came from analysts who were modelling our competitors or were modelling an IPO scenario for a spin-off from an existing competitor: in these cases they wanted forward-looking information about our business, but not to somehow re-perform the goodwill impairment test. This is a major reason why existing disclosures are somewhat minimalist and boiler-plate.

We do not think that investors want companies to make disclosures that would damage the value of their investments by allowing competitors to pre-emptively undermine the strategy behind the acquisition based on extensive and sensitive disclosures.

The proposals in DP include more of the same kind of potentially sensitive disclosures, and we note that the DP does not talk at all about reducing the disclosures in goodwill impairment in IAS 36, which cover some four pages in the standard.

Specifically:

- Publishing sales expectations of particular products or portfolios of products would be of great interest to competitors, as would any achievement or non-achievement of sales or growth targets.
- Similarly publishing expected timelines on research and development projects would be of interest, especially in business areas where time to market is an important economic consideration.
- Many acquisitions result in restructurings, either at the acquired company or the acquiring company (or both). Such restructurings may well include changes in headcount, and such changes need to be handled appropriately with the affected employees as well as with other bodies such as trades unions, works' councils, employee associations, etc. Requiring companies to quantify and describe so-

called "synergies" that may arise may well prejudice these discussions and may negatively impact the relationship between the company and its current and new employees.

(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?

Answer to Question 2e

There are very relevant and valid issues here, and it is concerning that some commentators seem to casually disregard them.

- Publishing targets for an acquisition, and then subsequently reporting on the achievement (or not) of these targets could well be regarded as "guidance" in many capital markets, and this may well include Switzerland. This would especially be the case for the large acquisitions that appear to be the main cause for concern, the targets here may well be material for the acquiring company as a whole. "Guidance" discussions are usually included in materials such as press releases and investor relations presentations; rarely are they included in a Management Discussion and Analysis and never in audited Financial Statements.
- Lawsuits can arise in the case of acquisitions of public companies, whereby the previous shareholders allege that the target's management "undersold" the company to the acquiring company. These lawsuits are typically directed at the acquiring company, as well as the management of the target company. Any targets and subsequent achievements published by the acquiring company for the acquisition may well get drawn into such litigation.
- Many acquisitions include earn-out clauses and contingent consideration arrangements. These are subject to various reviews, audits and, if needed, arbitration procedures agreed between the concerned parties. Again any targets and subsequent achievements published by the acquiring company for the acquisition may well get drawn into such procedures.
- The acquired company may have pre-existing relationships with other third parties, such as joint arrangements and alliance/licensing agreements. These may have

confidentiality clauses or requirements for published information to be pre-agreed. They may also include reviews, audits and, if needed, arbitration procedures.

- All of the above examples could have a negative impact on the company which would result in a loss of value to shareholders and investors.

Question 3 - Improving disclosures about acquisitions

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?

Answer to Question 3

The stakeholder feedback in DP 2.53 is unsurprising. Anyone who reads IFRS 3 B64-B67 would readily understand why the disclosures are prepared with a checklist approach. The checklist approach is driven heavily by auditors and regulators, and DP should be more balanced in the comments that it makes.

We would agree that the disclosure requirements in IFRS 3 should be reviewed and if necessary improved – not necessarily expanded. We believe that if users had a better understanding of what exactly was acquired and the rationale behind it, then this would reduce their appetite for subsequent reporting of the acquisition. They would have better information at the inception of the deal and would be able to do much more of the analysis themselves.

As noted elsewhere we do not support the inclusion of published targets and subsequent reporting in the financial statements. We believe such information, if needed, is more appropriately included in the Management Discussion and Analysis. Moreover the need for such governance and value-for-money reporting seems to us rather a matter for regulators than accounting standard setters.

SwissHoldings

Question 4 - Improving disclosures about acquisitions

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?

Answer to Question 4

The views and proposals in the DP are built on a fundamental misunderstanding of what the book value of goodwill on the balance sheet represents.

The goodwill number in the balance sheet is a mathematical residual. The goodwill per IFRS 3 is not a bottom-up calculation of discrete factors and it is not in any way part of the acquisition case considerations. There are a number of factors that play into the purchase price that a company is willing to pay for an acquisition. Some of these end up as separately recognised assets and liabilities on the balance sheet, and some remain unrecognised and hence roll into the residual goodwill. Goodwill can to some extent be rationalised in a qualitative manner but not quantitatively.

An acquisition may have synergies, most usually do. These may be revenue synergies or cost synergies. These are typically not known, or at least not reliably estimable, during the deal-making phase – any synergy considerations in the business case are often educated guesses rather than robust estimates. And what a company actually does after an acquisition has closed is frequently very different from what it planned to do while negotiating a deal.

Therefore except in case of large mergers of similarly sized entities, where synergy savings are a significant part of the deal rationale, there are not central synergy targets from acquisitions – synergies always exist to some extent, but in most cases they are incidental. The DP is proposing that companies disclose something that does not exist.

The kind of synergy reporting envisaged by the DP would in any case be highly judgemental and arbitrary. There is always an issue preparing alternative-reality accounting data: the actual numbers are clear, but to say what the numbers would have been had something different been done or how much of the results are attributable to a particular activity is very problematic, and also practically very difficult to audit. And the further the distance in time from the actual transaction the more difficult it would be to rationalise.

In general it makes good business sense to on-board new companies as quickly as possible and creating Us-&-Them reporting works against this. For day-to-day business the acquisition price is a sunk-cost and not relevant.

We would further note for example that there is no equivalent requirement to report targets and achievements from other activities, such as R&D or restructuring. It seems to us that the proposals are extending beyond financial accounting into governance and value-for-money considerations. We question whether such topics should be included in financial statements, and we believe these are rather governance issues for the regulatory authorities.

We can support that the DP would rather require companies to give qualitative information about synergies – what they are (revenue/cost), how they arise, and whether they are material or incidental to the transaction rationale. But publishing targets and reporting subsequent performance, if needed, should rather belong in the Management Discussion and Analysis, and as described above poses significant practical challenges.

We support the proposal to disclose pension and debt liabilities separately in the acquisition accounting disclosures.

SwissHoldings

Question 5 - Improving disclosures about acquisitions

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?

Answer to Question 5

a)

We do not object to this current requirement of IFRS 3. It is reasonably well-accepted and companies are generally able to prepare this. We are not aware that users find this disclosure particularly useful.

b)

In general providing more Illustrative Example and Implementation Guidance is always welcome. It seems to us that this is a better approach to help preparers apply their judgment, rather than issuing additional requirements to try and legislate for good judgement.

We can see that it may be helpful that companies outline the assumptions used in preparing the pro-forma disclosures. The risk is that a detailed list of requirements in a standard could mushroom into a large boiler-plate disclosure, such as are often seen in disclosures on goodwill impairment, pensions or stock options. If the IASB can develop reasonable practical proposals, we would support this.

c)

We do not support these proposals. We believe the existing disclosures are sufficient, if well-prepared and well-explained.

With ‘operating profit before acquisition-related transaction and integration costs” the DP is creating another Alternative Performance Metric. It is unclear how this APM is to be calculated, for example whether it includes transaction and integration costs incurred by the acquired company or by the wider business. As noted in our comment letter to the ED on “General Presentation and Disclosure”, we have reservations about the proposed definition of Operating Profit in the ED. In practice most users will be more interested in the impact on the company’s current APMs in any pro-forma information.

In practice it would be extremely difficult to derive pro-forma cash flows. The data to this would not be easily available, and the production of such numbers would require a considerable amount of judgement and arbitrary allocations. For example cash flow from operations per IAS 7 includes income taxes, and post-acquisition the acquired company will typically become part of a group tax filing. How are the income tax cash flows supposed to be calculated? The information would be of limited value and would be borderline unauditable.

SwissHoldings

Question 6 - Goodwill impairment and amortisation

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?

Answer to Question 6

We believe that, in general, the impairment testing process set out in IAS 36 works well. This is evidenced by it being reasonably well-accepted and there being relatively few complaints about IAS 36 when it is applied to Property, Plant and Equipment and also to individual Intangible Assets. The problems come when IAS 36 is applied to goodwill. We would say that the problem that needs fixing is the accounting for goodwill generally rather than impairment testing per IAS 36.

It seems to us that there is a large expectations gap created by the accounting profession collectively about financial reporting for M&A activities generally and about goodwill specifically.

- A particular M&A transaction may under-achieve, relative to the deal cost, for any number of reasons. These can include lower than expected revenues, higher than expected costs, technical obsolescence or failure of acquired intellectual property, delays, competitor pressure, regulatory changes etc.

- The goodwill number in the balance sheet is a mathematical residual calculated by taking the IFRS3-defined cost of acquisition (which is different from the deal price) and subtracting the IFRS3-defined net assets acquired (which is different from the value ascribed to these net assets during the M&A process).
- This goodwill is then allocated to a cash-generating unit and tested for impairment per IAS 36. An impairment arises when the recoverable amount (usually the value-in-use estimated by the company) is lower than the carrying value of the assets in the cash-generating unit.

It will be completely coincidental if the goodwill impairment calculated in the last bullet occurs at the same time, if at all, as the under-achievement set out in the first bullet. Rather than ask about "too-little-too-late" we could reframe the question to ask "why should we expect that goodwill impairment should happen at the same time as under-achievement of an M&A deal". The reality is that there is no reason why it should.

Of course management over-optimism in the impairment process can lead to a delay in recognition of impairment losses. In our experience these assumptions are heavily audited and this effect is over-emphasised by critics of the impairment process. Even if the alleged management over-optimism could be somehow magically eliminated, we would still be facing the same complaints about goodwill impairment.

The shielding issue is structural in the design of goodwill impairment testing set out in IAS 36. This is implicit from the truism that the book value of goodwill does not generate cash in and of itself and therefore cannot be tested for impairment on its own. If we take it to a logical extreme and allocate goodwill only to a CGU of the business activities of the acquired company (without any consideration of the wider benefits) then in many cases the goodwill would be impaired immediately after the deal closes. Indeed it can be questioned whether it is even appropriate to show goodwill as an asset on the balance sheet.

There is a converse of the shielding issue, which is less commonly seen. If goodwill from an M&A deal that is high-risk-high-reward it is allocated to a cash-generating-unit with similarly profiled assets already owned by the company, then there is a risk of goodwill impairment even if the M&A deal itself is working out just fine: an underachievement in the other "legacy" assets in the CGU could lead to a goodwill

impairment. The reason this is less commonly seen is such underperforming CGUs would likely have been impaired already, or that preparers are mindful when allocating goodwill to CGUs that they do not create this situation.
In conclusion we believe that the goodwill impairment testing as currently set out in IAS 36 is designed-to-fail. It cannot reasonably be expected to meet the expectations of shareholders and investors, and no amount of tweaking of IAS 36 is going to change that. Therefore we agree that with the IASB's conclusion in the DP that the current impairment testing for goodwill in IAS 36 cannot be reasonably improved to make it more effective. We would rather say it cannot be reasonably improved to make it less ineffective.

We would recommend to leave IAS 36 as it is, and rather, as part of a wider project on "Intangible Assets", to reopen the accounting treatment of goodwill from end-to-end, including consideration of whether it should even be recognised on the balance sheet in the first place, and if so, how should it be subsequently treated.

Question 7 - Goodwill impairment and amortisation

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 amortisation 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?

Answer to Question 7

a)

The accounting for goodwill, and intangible assets in general, is in our view a wider project that the IASB should prioritise as a matter of urgency. As part of such a project the accounting for goodwill should be revisited, including recognition (if at all), measurement, subsequent treatment in the P&L, and disclosure; and including a consistent treatment of internally generated goodwill and goodwill from business combinations.

Having said that, views on goodwill amortisation versus the impairment-only model are strongly held, and there are views in both camps. That is true for the members of SwissHoldings as much as for other bodies.

A discussion on this narrow aspect can be held. But in our view such a discussion would not be especially productive and would consume time and intellectual and emotional energy – and the end result would continue to leave one side or the other unhappy.

Whether we use goodwill amortisation or impairment-only does not really matter much in the real world. Users are well aware of the shortcomings of the current model and goodwill accounting generally, and everyone has work-arounds. Balance sheet and income statement entries for goodwill are routinely ignored and adjusted out – so replacing one method with another does not change anything. The information provided to users does not become more useful either way, it rather remains equally useless.

b)

We are not aware of significant new evidence one way or another. We would observe that the continuing complaints and challenges to the current goodwill impairment process are ample evidence that all is not well, and the current model is not achieving what users expect that it would.

In reality this discussion has not been evidence-based. As far as we recall the switch in IFRS in 2004 from amortisation to impairment-only was driven primarily by convergence considerations and discussions with FASB on M&A accounting generally, including merger accounting. We do not recall a ground-swell of evidence in 2004 supporting the impairment-only model – it was rather sold as being a necessary step to achieve convergence.

As noted, and as we are sure the IASB is aware, views on this topic are strongly held. In general if people hold a particular views from an emotional or faith-based perspective then providing logical evidence is usually not going to change their minds.

c)

The reintroduction of amortisation would obviously have a mathematical impact on the impairment of goodwill. It would logically lead to a less impairments. It does not change the underlying structural issues with goodwill impairment testing.

d)

We do not calculate or measure so-called “internally generated goodwill” in our internal reporting. Goodwill exists on the balance sheet only as an accounting concept arising from IFRS 3.

e)

Without doubt, if amortisation of goodwill were to be reintroduced then this would be immediately “adjusted out” in most non-GAAP metrics, in the same way that goodwill impairments are. Even if preparers would not do this, their users would demand it.

In our experience goodwill impairment is the mostly commonly adjusted item in non-GAAP metrics. Investors, analysts, ratings agencies and lenders almost always strip out goodwill from their models, both on the balance sheet and in the income statement. Similarly it is routinely adjusted out in the internal management reporting.

The reason for this is that goodwill is not accepted as an “asset”, in the normal meaning of the word, and is rather an arbitrary residual on the balance sheet. To the extent users want to make judgements on the company’s M&A strategy, this is a separate discussion and different information and analysis is used.

This is implicitly recognised by the IASB in DP, with the proposals in pp3.107–3.114 about requiring companies to present on their balance sheets the amount of total equity excluding goodwill.

f)

If amortisation of goodwill were to be reintroduced, we believe that the original procedures from IAS 22 are as good as any. Any useful life would be to some extent arbitrary, but having a rebuttable 20 year cap seems a reasonable approach.
We do not believe that the book value of goodwill on the balance sheet or the subsequent impairment/amortisation give useful information to investors. Therefore bringing back amortisation would not make any difference in this respect.

Question 8 - Goodwill impairment and amortisation

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?

Answer to Question 8

a)

We find this proposal unnecessary. Obviously users are able to very simply deduct the balance sheet value of goodwill from the balance sheet value of equity, should they wish to do so. The proposals in the recent ED on General Presentation and Disclosures would require goodwill to be shown as a separate line item on the face of the balance sheet, so this calculation would become even easier if those proposals are adopted.

As an aside, we note again that the recent ED on *General Presentation and Disclosures* **prohibits** companies that use the functional method of income statement presentation from showing goodwill impairment on the face of the income statement, while at the same time making it **compulsory** to show goodwill on the face on the balance sheet. The DP now doubles-down on this by proposing to require disclosure of this new metric, equity excluding goodwill.

Underlying this, there is a rather disturbing passive-aggressive approach to financial reporting. It is as if we are saying "goodwill isn't a real asset, but we have to put it on the balance sheet – but just in case, here is the equity number excluding goodwill, so don't blame us if this goodwill later turns out to be valueless". As noted elsewhere, we would rather propose that the current project broaden to include a fundamental review of then financial accounting model for intangible assets, including goodwill. Fix the accounting not the disclosure.

b)

We believe this proposal should be dropped.

Question 9 - Simplifying the impairment test

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?

Answer to Question 9

We appreciate the IASB's effort to simplify the process. However we believe that this proposal will not substantially improve the process, and that many preparers will continue with the existing process which has already been set up. The reasons for this are two-fold:

- The goodwill impairment testing process is highly specific and is not a routine process. It needs to be planned and scheduled and the necessary resources need to be assigned. If the test was only needed on an ad-hoc basis based on a trigger test, then it would not be a straight-forward process to mobilise the necessary resources at short notice. Much of the expertise and knowledge might be lost if not regularly utilised.
- It is debatable whether having a trigger test then targeted impairment test process is simpler or cheaper than simply having an obligatory annual impairment test. The process and documentation needed for the trigger test would be quite burdensome, given the high focus given to this topic by auditors and regulators. It would likely be simpler just to do the impairment test anyway, which can be more easily and efficiently planned and organised. Therefore, the planned simplifications would have limited impact in practice.

SwissHoldings

We do not believe this proposal would fundamentally change the robustness of the impairment testing per se. As noted above, it may actually make it worse due to a loss of expertise and process know-how in companies.

Question 10 - Simplifying the impairment test

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.

Answer to Question 10

a)

These proposals are welcome and would simplify the impairment process. The proposal to permit the value in use test to consider realistic plans for the CGU is simply an acknowledgement of the way that a business actually plans to use its assets, and would avoid non-value-added adjustments to the real plans of management. Using post-tax discount rates would be particularly appreciated and would correct a well-known and long-standing defect in IAS 36. As pp4.46 of the DP notes, post-tax rates are commonly used in valuations, and these are the basis of observable market rates.

b)

We do not see the need to develop specific guidance on "discipline". In our view this is implicitly required in all financial reporting. As noted in earlier answers the observed issues with testing goodwill under IAS 36 are structural and are not primarily due to over-optimism or lack of discipline on the part of preparers.

SwissHoldings

Question 11 - Simplifying the impairment test

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?

(b) 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? Paragraphs BC145–BC180 of the Basis for Conclusions describe the Board's reasons for the proposals and discuss approaches that were considered but rejected by the Board.

Answer to Question 11

a)

In general providing more Illustrative Example and Implementation Guidance is always welcome. It seems to us that this is a better approach to help preparers apply their judgment, rather than issuing additional requirements to try and legislate for good judgement.

Allocating goodwill to segment level only, as discussed in pp4.55 (c), would undoubtedly simplify the impairment testing process. This would however have the consequence of magnifying the so-called "shielding effect" that many commentators criticise.

We would not support the ideas expressed in pp 4.55(b). We believe that IAS 36 should continue to use recoverable amount, being the higher of value-in-use or fair-value-less-cost-to-sell. In certain cases fair-value-less-cost-to-sell is relatively easy to calculate and can simply demonstrate that the recoverable amount is higher than the carrying value – this obviates the need to carry out a complex value-in-use calculation. An example of this is where the goodwill arises from the acquisition of a majority stake in a company where the minority is publicly-quoted – market value of the majority stake is easy to calculate (and audit) in this circumstance.

b)

In the first part of the DP, the IASB sets out new proposals for the reporting of objectives and subsequent performance of acquisitions. The reason is partly due to dissatisfaction with the goodwill impairment process. We would therefore expect that if new more-useful disclosures are being proposed then existing less-useful can be discontinued. IAS 36 is notoriously disclosure-heavy in the area of goodwill impairments, with the goodwill specific disclosures in IAS 36 pp134 – pp137 spreading over nearly four pages, and this is not counting the further six pages of the Illustrative Example 9.

SwissHoldings

Question 12 – Intangible Assets

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?

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

Answer to Question 12

These are very valid points to discuss. However, we agree that this topic should not be taken up at this stage. We would rather see this as part of wider project to look at the financial accounting for intangible assets, including goodwill, not only in the context of business combinations but also for internally generated assets.

Question 13 – Other Recent Publications

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?

Answer to Question 13

As noted previously, we believe that additional disclosures on the objectives, targets and subsequent performance of business combinations:

- Are best addressed as a global regulatory level to ensure a level playing field, especially between IFRS preparers and their competitors who may be using US, Chinese or other standards. To impose these at an IFRS level only would create a competitive disadvantage.
- Should be placed in the Management Discussion and Analysis and not in the Financial Statements.

Our comments on the accounting treatment of goodwill are independent of what the FASB may or may not do. We believe that there is considerable merit in a project to fundamentally review the accounting for intangible assets, including goodwill, and ideally this would be a project that the IASB and FASB can work jointly on, as the concerns are the same in both financial reporting regimes. However if the FASB choose not to engage on this topic, we believe the IASB should anyway take this up.

SwissHoldings

Question 14 – Other comments

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?

Answer to Question 14

1) Interim Reporting

   We appreciate that this is only a Discussion Paper and not an Exposure Draft. However we could not find any reference in the DP to what disclosures would be required for interim reporting, notably for the additional disclosures on the objectives, targets and subsequent performance of business combinations. Many preparers are concerned by this, as currently IFRS 3 has the most onerous interim disclosure requirements of any standard, in effect requiring full year-end disclosure in interim reporting. We recommend that in the next iteration of these proposals, it is made explicit what exactly is and is not required in interim reporting.

2) Scope of Companies affected

   The rationale for the proposed additional disclosures on the objectives, targets and subsequent performance of business combinations, as set out in pp1.7 and elsewhere in the DP focuses on the needs of investors for these disclosures. Therefore we would recommend that private companies and subsidiaries be scoped out of these requirements. We refer to IAS 33 pp2, where a similar exemption is made for Earnings Per Share requirements.

3) Change overload

   We would draw the IASB's attention to the current economic environment at the end of 2020. Many companies, large and small, are facing an extremely difficult business conditions. It is a challenge to product financial statements in this situation, just as it is a challenge for auditors and regulators. In addition internal company budgets for areas such as Finance and IT are under pressure.

   In this situation the IASB should be cognisant not to unnecessarily increase the burden by introducing additional disclosures without deleting no-longer useful disclosure and by changing the accounting rules for non-critical matters.

We would encourage the IASB to focus its efforts on the things that need fixing, and to have in mind the issue of disclosure overload. A default mindset of one-in-one-out for disclosure changes would be most welcome and is, in our view, of increasing necessity.