STAFF PAPER

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IASB Meeting

Project	**Post-implementation review IFRS 3 *Business Combinations***
Paper topic	Summary of comments received

CONTACT(S) Leonardo Piombino lpiombino@ifrs.org +39 06 6976 6834

Introduction and purpose of this paper

1. This paper summarises the information received in response to the IASB's Request for Information *Post-implementation Review: IFRS 3 Business Combinations* (the 'RFI'). The RFI was published for public comment in January 2014; the comment period ended on 30 May 2014. The IASB received 93 comment letters in response to the RFI. In addition, the IASB and staff took part in 30 outreach activities in order to gather feedback on the issues included in the RFI. This summary is based on the staff's preliminary analysis of comment letters as well as on information received from outreach activities.
2. This paper will ask the IASB whether we have received enough information to prepare a Feedback Statement on the implementation of IFRS 3. The IASB will not be asked to make any technical decisions at this meeting.

Integration of messages received

3. The messages received are generally similar, whether they arise from outreach activities or through formal comment letters. Consequently, respondents to the RFI and participants in outreach activities are referred to as 'participants' throughout the paper.
4. For further details on the respondents to the RFI and the participants in outreach activities please see Appendix A of this paper.

Issues included in the RFI

5. The RFI asked about the following issues:

   (a) definition of a business;

   (b) fair value measurement;

   (c) separate recognition of intangible assets from goodwill and the accounting for negative goodwill;

   (d) non-amortisation of goodwill and indefinite-life Intangible assets;

   (e) non-controlling interests;

   (f) step acquisitions and loss of control;

   (g) disclosures;

   (h) other matters; and

   (i) effects.

6. In the following paragraphs we provide a summary of the comments received on each of the questions asked in the RFI.

Comments received

General comments

7. Many participants support performing Post-implementation Reviews as an opportunity to assess the effects of Standards on financial statements and their evaluation by various stakeholders.

8. Many participants think that, overall, IFRS 3 as currently drafted achieves its objectives and works well; however, there are some areas in which practical issues have arisen and where further clarification would be useful.

9. Some respondents[1] noted that:

   (a) although many preparers acknowledge the conceptual merits of the overall acquisition accounting model in IFRS, most expressed

[1] See, for example, EFRAG's comment letter.

significant concerns regarding the level of effort required and costs incurred to meet its requirements. Many preparers question whether the increase in costs has exceeded the benefits to users.

(b) the users we spoke to say that they take a holistic perspective when analysing a business combination, and tend to focus primarily on the 'entirety' of what had been acquired for the consideration paid, instead of on the individual assets acquired and liabilities assumed. Consequently, in several cases, users request rather different information than that required by the Standards. Users commented that information about business combinations was often scattered in the financial statements and that they need information on the day that the deal is announced to keep abreast with market reactions. Some of these users raised the need for improvements to IAS 34 *Interim Financial Reporting* with regards to information on business combinations.

10. Some respondents[2] think that the accounting requirements introduced in IFRS 3 have not achieved improvements from a cost-benefit perspective in all aspects and that changes are necessary to address these cost-benefit concerns.

11. ASCG foresees potential conflicts between the current measurement principle (and corresponding guidance) underlying IFRS 3 and the IASB's preliminary view developed in the Discussion Paper for measurement guidance in a revised *Conceptual Framework*. In their view, the proposals in the *Conceptual Framework* emphasise a closer linkage of measurement with the way that the assets are used within the entity and how they will contribute to future cash flows. Consequently, they think that current guidance in IFRS 3 requiring the highest and best-use perspective of other market participants could be considered as inconsistent with the thinking for a revised *Conceptual Framework* regarding the selection of measurement.

12. Other respondents[3] support the general approach in IFRS 3 of accounting for business combinations and think that although various improvements could be made to IFRS 3, major revisions are not required and thus a major project is not

[2] See, for example, ASCG's comment letter.

[3] See, for example, AASB's comment letter.

warranted. They also think that any decision by the IASB to establish a standard-setting project arising out of the PIR should be made in the context of its periodic agenda consultation, so that competing priorities can be properly considered.

13. Some respondents[4] think that the IASB should seek to work together with the Financial Accounting Standards Board (FASB) to the extent that future changes are considered in order to mitigate the risk of divergence in this important area. They note that the FASB has recently decided to reconsider the post-acquisition accounting for goodwill, and they would support a similar effort by the IASB.

14. Some respondents[5] think that IFRS 3 does not serve either preparers or users well. Both groups frequently adjust the accounting numbers derived from the application of IFRS 3 to provide metrics that they think better portray the economic reality of business performance. They claim that Standard generally fails to provide users with decision useful information or information that helps users hold management to account. They observed that while the application of IFRS 3 imposes significant costs on preparers, there is also a meaningful cost to investors as they seek to unravel the numbers produced by the Standard. Additionally, given the difficulties that investors often face interpreting this Standard, in their view, it is likely that it distorts the efficient operation of capital markets.

15. Others[6] think that investors and analysts are increasingly familiar with the requirements of IFRS 3 and better able to interpret and evaluate transactions reported under this Standard.

16. Many participants[7] encourage the IASB to complete its project on business combinations under common control.

[4] See, for example, PWC and DT comment letters.

[5] See, for example, Henderson Global Investors' comment letter.

[6] See, for example, Anglo American Platinum Limited's comment letter.

[7] See, for example, CINIF's comment letter.

Definition of a business

Are there benefits of having separate accounting treatments for business combinations and asset acquisitions? If so, what are these benefits?

17. Most participants think that there are benefits of having separate accounting treatments for business combinations and asset acquisitions. The main benefits claimed by participants are the following:

    (a) management has to render account for the business combination made and the value drivers behind.[8]

    (b) the distinction between a business combination and an asset deal makes sense, because a business should be worth more than the sum of its parts.[9] This justifies the recognition of goodwill.

    (c) having different accounting outcomes is appropriate because of the different nature/economic substance of the transactions.[10]

    (d) asset acquisitions are more prevalent and require a simpler and more understandable accounting treatment. The historical cost accounting approach is more appropriate for frequent and routine transactions. Business combinations are generally less frequent and more complex, and require a different approach that includes consideration of factors, such as value of consideration, identification and valuation of assets and liabilities acquired and the existence of goodwill.[11]

    (e) business combination accounting gives a clear view on the evaluation of the new business and its impact on the combined entity. It conveys a better understanding of the underlying transactions to users of financial statement.[12]

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[8] See, for example, Linde Group's comment letter.

[9] See, for example, Six Swiss Exchange's comment letter.

[10] See, for example, FRC and ICAEW's comment letters.

[11] See, for example, Astra Zeneca's comment letter.

[12] See, for example, FRC Mauritius's comment letter.

(f) the advantage of having business combination accounting (as opposed to using asset acquisition accounting) for large transactions is that, it forces management to more closely consider the acquisition price, because management has to identify the assets/liabilities and goodwill being acquired, and the synergies that justify paying the premium that forms part of goodwill.[13]

18. Many participants[14] think that a separate accounting treatment is conceptually justified only with respect to goodwill; they do not see convincing reasons for the other accounting differences. They recommend the IASB to revisit whether the separate accounting treatment of deferred tax, contingent payments and acquisition costs is really justified, taking into consideration the difficulties that arise from having to determine whether a transaction represents an acquisition of assets or a business combination.

19. Some participants[15] have not identified any benefits of having separate accounting treatments for business combinations and asset acquisitions. They do not view recognition of goodwill as a 'separate accounting treatment' for business combinations and asset acquisitions. They think that whether goodwill can exist in an asset acquisition or only in a business combination depends on the definition of a business and that using the current definition of a business, the existence of goodwill in an asset acquisition would be very unlikely. They also think that if goodwill occurs only in a business combination, then the use of goodwill accounting for business combinations does not represent a separate accounting treatment for business combinations versus asset acquisitions, but the accounting for an asset that is unique to business combinations. If goodwill were to occur in an asset acquisition, they see no conceptual argument for not recognising it or not accounting for it in a manner consistent with that required for a business combination.

[13] See, for example, CFA UK's comment letter.

[14] See, for example, FEE's comment letter.

[15] See, for example, ACSB's comment letter.

What are the main practical implementation, auditing or enforcement challenges you face when assessing a transaction to determine whether it is a business? For the practical implementation challenges that you have indicated, what are the main considerations that you take into account in your assessment?

20. The main challenges participants said that they faced when determining whether an acquisition includes a business are the following:

(a) the assessment of the relevance of processes acquired as part of the acquired set of assets and significance of the processes missing from the set. This is particularly the case when only some of the processes are being acquired and it is necessary to determine whether the processes that are acquired (and those missing) are necessary to the production of outputs or are merely administrative processes.[16]

(b) a challenge can arise when the acquisition is a combination of assets and a business (ie multiple projects acquired at different stages of development). Some participants commented that it may be appropriate to apply the accounting relevant to the dominant element or to bifurcate the transaction into an asset and a business. [17]

(c) the definition of a business is too broad and IFRS 3 has little or no guidance on when an acquired set of assets is not a business. This can make it difficult to distinguish between an asset deal and a business combination[18].

(d) the wording 'capable of being conducted as a business' does not help in determining what transaction is actually a business that deserves the specific business combination accounting treatment.[19]

(e) clarity is required on the definition of a business when the entity acquired does not generate revenues.[20]

[16] See, for example, FEE's comment letter.

[17] See, for example, BP's comment letter.

[18] See, for example, Sanofi-aventis's comment letter.

[19] See, for example, Sanofi-aventis's comment letter.

(f) issues arise in practice because the application guidance in Appendix B of IFRS 3 uses terminology different from the definition in Appendix A; it introduces the idea that a business does not need to contain all its elements, such as to create a second definition that is sometimes vague and appears all-embracing. The impact is that Appendix B appears to imply that a business could merely be an asset, leaving several questions open.[21]

(g) the term 'market participant' is not defined in IFRS 3. Some sets of activities and assets may be considered a business for a specific group of market participants if they could integrate the set of activities and assets in their processes. However, the same set of activities and assets might not be considered as a business from the perspective of other market participants. Further guidance on what constitutes a market participant would help in this determination.[22]

(h) when some of the acquiree's processes and activities were outsourced to third parties before an acquisition, it is unclear whether some or all of the related contracts need to be taken over by the acquirer for the transaction to be considered an acquisition of a business[23].

(i) an entity might enter into an asset acquisition agreement with another entity. With a separate agreement that results in processes being acquired, such as a supply agreement or research and development agreement. When the asset acquisition agreement and the separate agreement on processes are considered together, the acquisition may be classified as a business. Disagreements can arise in practice about whether to treat the two agreements as a single transaction for purposes of deciding whether there is an acquisition of a business.[24]

[20] See, for example, Meyers Norris Penny's comment letter.

[21] See, for example, KPMG's comment letter

[22] See, for example, EY's comment letter.

[23] See, for example, ACSB's comment letter.

[24] See, for example, ACSB's comment letter.

(j) the main practical challenge in determining whether a transaction should be accounted for as a business combination instead of an asset purchase is the fact that the assessment is primarily fact driven, instead of taking the business rationale, the strategic considerations and objectives of the acquirer into account.[25]

21. The main considerations that participants said that they take into account in determining whether an acquisition includes a business are the following:

(a) the transfer of a significant number of employees often indicates that the transaction is a business combination.[26]

(b) some respondents described a pragmatic approach to test whether a group of assets could be considered as a business is to answer these questions:

(i) could this group of assets work independently?

(ii) could this group of assets have a market to sell its products?

(iii) does this group of assets have its own managers and separate accounting?[27]

(c) some respondents think that the differentiator between an asset and a business is more in relation to the presence or absence of activities and processes. When applying the term ‘capable’, they usually look at both their business model and that of the seller, because, in their view, most assets can be turned into a business if the business model is buying and selling assets. They also think that the capability of integrating any acquired asset with the existing processes and people of the acquirer is not considered to be sufficient to treat an acquisition as a business combination.[28]

[25] See, for example, Allianz’s comment letter.

[26] See, for example, Astra Zeneca’s comment letter.

[27] See, for example, American Appraisal’s comment letter.

[28] See, for example, BP’s comment letter.

(d) an approach to evaluate whether additional services to generate cash flows could be easily provided by third parties. If so, some[29] think that under the current interpretation this would be a rebuttable presumption to account for a business combination.

(e) the purpose of the acquisition (for example, whether the transaction is to maximise investment return and collect cash flows over a certain investment period) and the primary benefits for the acquirer (for example, whether the transaction provides other beneficial 'resources' that go beyond the identifiable assets of the acquire, for example, by integrating the acquiree in the acquirer's own business activities) should be considered in determining whether the transaction is a business combination.[30]

22. Many participants think that applying the definition of a business is particularly challenging in some industries, such as real estate, extractive, pharmaceutical, technology and shipping.

23. Some participants[31] say that they have observed diversity in practice in interpreting the term 'business'. They think that in the USA the majority of the transactions are accounted for as business combinations whereas in Europe the majority are accounted for as an asset acquisition.

24. Many participants[32] encouraged the IASB to reconsider the scope of the definition of a business and provide more guidance and clarification as to what constitutes a business.

Fair value

To what extent is the information derived from the fair value measurements relevant and the information disclosed about fair value measurements sufficient? If there are deficiencies, what are they?

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[29] See, for example, Bayer's comment letter.

[30] See, for example, Allianz's comment letter.

[31] See, for example, German Property Federation's comment letter.

[32] See, for example, EFRAG's comment letter.

25. Many users think that fair values at the acquisition date provide useful information about how management spends the investors' money. They think that fair value is the best approach for measuring the assets acquired and liabilities assumed in a business combination, even though fair value does not facilitate the comparison of trends between companies that grow organically and those that grow through acquisitions.

26. However, some users think that in many cases the allocation of the purchase price to the individual assets acquired and liabilities assumed is subjective. They think that it would be useful to have more information on how fair values are determined (ie inputs and assumptions used in the valuations).

27. Some analysts do not agree with upwardly revaluations of acquired inventory to fair value and usually ignore these adjustments from their measure of underlying earnings. The reduced profitability in the first period following the acquisition is not viewed as sustainable or recurring. Although they understand the rationale for writing inventory up to the current market value, they think that in practice no one would pay full value for stock that they were going to trade out post acquisition because there would be no profit.

28. Some users indicated that it would be useful to have information on both the acquisition-date fair values and the pre-acquisition book values of assets acquired and liabilities assumed.

29. Some users think that fair value measurements are useful when asking management questions and to understand better the transaction.

What have been the most significant valuation challenges in measuring fair value within the context of business combination accounting? What have been the most significant challenges when auditing or enforcing those fair value measurements? Has fair value measurement been more challenging for particular elements?

30. Many preparers[33] think that the calculations are often difficult to prepare, taking a significant amount of time and often require the engagement of independent valuation specialists, which makes the exercise costly.

[33] See, for example, The 100 Group's comment letter.

31. Many participants[34] think that the biggest valuation challenge is the identification and measurement of intangible assets that are separable from goodwill. This is primarily due to the lack of sufficient reliable and observable data. Intangible assets that are particularly challenging to measure are: non-contractual intangible assets; intangible assets for which there is no active market; and intangible assets in the 'early stage' of development. In addition, where there are multiple intangible assets, such as brand names, customer relationships and customer lists, judgement is needed not only to value them individually but also to determine interrelationships.

32. Some preparers[35] think that the most significant challenge is the application of the different types of asset valuation methods and the determination of the respective input parameters. In their view, the underlying problem is that the Standards refer to a valuation model ('stand-alone fair values' defined as price paid in an arm's length transaction) that are hardly applicable in practice, because it does not exist for most assets being too specific for having observable transaction or market prices.

33. Many participants[36] think that the fair value of contingent consideration is highly judgemental and difficult to validate. This is particularly relevant in the healthcare industry, whereby the research and development period of a drug can take more than a decade to get a preclinical compound to market. In this industry, it is common for deal structures to have multiple success-based contingent consideration payments linked to the successful completion of the various phases of the research and development process. Given this, they think that it is extremely challenging to fair value these contingent payments at acquisition (or within 12 months of acquisition date) based on the probability of success of each milestone.

34. Some preparers[37] think that the most significant challenges are:

(a) unintentional consequences of fair valuing long term provisions ('Day 2' implications). In applying the acquisition method, provisions are

[34] See, for example, American Appraisal's comment letter.

[35] See, for example, Linde Group's comment letter.

[36] See, for example, Roche Group's comment letter.

[37] See, for example, CFO Forum South Africa's comment letter.

measured at acquisition-date fair value. Subsequently, provisions are recognised and measured in accordance with IAS 37 *Provisions, Contingent Liabilities and Contingent Assets* (ie not at fair value). Due to the different measurement requirements of IFRS 3 and IAS 37 this could result in a significant change in the provision and therefore an impact on profit and loss after the acquisition date.

(b) a similar mismatch arises with, for example, contracts that are unfavourable but not onerous. A liability for the unfavourable element is required to be recognised at the acquisition date. However, subsequently, and due to the fact that the contract is not onerous, the liability created is derecognised through profit and loss.

35. Some advisory firms[38] think that practical problems include isolating reliable revenue streams on which to base the valuation model; attributing costs; assessing value in the context of the new owner's strategies; and assessing contingent outcomes.

36. The most significant valuation and auditing[39] challenges in fair value measurement identified by respondents are:

(a) contingent consideration—due to the complexities and uncertainties in the arrangements, it can be difficult to determine the fair value.

(b) contingent liabilities—a number of different valuation approaches are used and, due to the uncertainties regarding outcomes, it is often difficult to determine the fair value as it is reliant on a number of assumptions.

(c) valuation of separate intangible assets—due to the number of valuation approaches and the level of judgement required. In most cases, these assets do not derive separate cash flows and determining their fair value requires a number of difficult assumptions to be made.

(d) step acquisitions—it can be difficult to fair value the existing equity investment when the shares are not quoted. For example, if the entity

[38] See, for example, Westworth Kemp Consultants' comment letter.

[39] See, for example, EY's comment letter.

previously held an investment of 20 per cent, should the investment be valued on the basis of a 20 per cent investment or should it be 20 per cent of the total value (which may include a control premium)?

(e) non-controlling interests—if there is no quoted price available, it may be difficult to determine a per-share value due to any control premium that may be included in the fair value of the controlling interest.

(f) financial liabilities—the announcement of a business combination may affect the quoted price of listed financial liabilities as a result of perceived credit enhancements provided by the acquirer or a perceived decrease in non-performance risk. The quoted price may be used as a level one fair value measurement to determine the fair value of the financial liability at the date of obtaining control. Should similar adjustments relating to perceived credit enhancements be recognised in determining the fair value of non-listed financial liabilities and, if so, how?

(g) equity consideration—in many instances, there is a delay between the announcement of a business combination transaction and the date that control is obtained. When the consideration is in the form of equity shares in a listed entity, the share price will often reflect the market's expectation of the transaction occurring, and the value of expected synergies, prior to the date that control is acquired. This means that measuring the equity at the fair value on the date of the acquisition may not accurately reflect the transaction that was agreed between the parties.

37. Many participants think that fair value measurement is more challenging for the following elements:

(a) non-contractual intangible assets;

(b) intangible assets for which there is no active market;

(c) intangible assets in the 'early stage' of development;

(d) contingent consideration;

(e) contingent liabilities; and

(f) inventory (because of the limited guidance provided).

Separate recognition of intangible assets from goodwill and the accounting for negative goodwill

Do you find the separate recognition of intangible assets useful? If so, why? How does it contribute to your understanding and analysis of the acquired business? Do you think changes are needed and, if so, what are they and why?

38. Some users[40] do not support the current practice of identifying additional intangible assets (brands, customer relations, etc) beyond goodwill, because the valuation of these assets is highly subjective and, in fact, open to significant arbitrage opportunities for companies during business combinations. They think that these intangible assets should be recognised only if there is a market for them.

39. Some users[41] think that:

(a) the separate recognition of intangible assets is of limited (if any) utility to investors.

(b) investors are interested in understanding the return on the capital (cash and cash equivalents) that has been deployed.

(c) investors give little credence to the valuations placed on acquired intangible assets, such as customer lists and brands.

(d) the subsequent accounting treatment of intangible assets acquired in business combinations is an unhelpful element of IFRS based accounting that investors face today. They think that it causes confusion, limits comparability and potentially distorts the efficient operation of capital markets.

(e) in most circumstances, the amortisation of acquired intangibles conveys no useful information about the economics of a business. It is normally added back by preparers and investors to derive an underlying earnings number. The number added back is sometimes referred to as purchase

[40] See, for example, SFAS's comment letter.

[41] See, for example, Enderson Global Investors's comment letter.

price allocation (PPA) amortisation. However, it is not always easy for investors to differentiate between PPA amortisation and the amortisation of other internally generated assets, such as capitalised software. The latter is more akin to depreciation and should not be added back to derive an underlying earnings number.

40. Similarly, some users[42] think that the amortisation charge arising from intangible assets, such as brands and customer lists, appears to be double counting, because the maintenance of these assets is already expensed through the income statement as another cost, such as sales and marketing. As such, many analysts add back these amortisation charges in their measures of underlying earnings. They would prefer that difficult-to-define (or difficult-to-separate from the overall business) and 'indefinite-lived' intangible assets, such as brands and customer relationships, should be subsumed into goodwill because they are more akin to goodwill. They think that only intangible assets that are contractual have a finite life and that are separate from the overall business (such as licences) should be recognised and measured separately. Separate recognition for such assets is useful, because they require large capital expenditure to be replaced. In their view, the recognition and amortisation of these assets is appropriate, because it is a proxy for the replacement cost of the asset.

41. The research published by the UK's Financial Reporting Council in March ('Investor Views on Intangible Assets and their Amortisation') identifies a distinction between 'wasting' intangible assets and 'organically replaced' intangible assets. Wasting assets have finite economic lives and would include licences, patents and software. Organically replaced assets are likely to be difficult to separate from the business or to reliably determine a useful life. Such intangible assets, including customer lists and brands, are replenished through marketing and promotional investment that is expensed through the profit and loss.

42. Some users[43] think that estimating fair values for intangible assets acquired in business combinations is a costly exercise for preparers and its advantage can be questioned. In their experience as analysts they rarely look at the values

[42] See, for example, CFA UK's comment letter.

[43] See, for example, EFFAS's comment letter.

accounted for. An exception would be for those intangible assets for which a reliable measure of fair value can be attained.

43. Some users think that intangible assets that are tax deductible should be separated, because they are useful to estimate future tax expenses.

44. However, other users think that the separate recognition of intangible assets from goodwill is useful, because

(a) it provides an insight on why a company purchased another company and provides information on the future cash flows arising from the acquired business.

(b) it helps in understanding the components of the acquired business, including its primary assets (ie the value-drivers).

(c) it permits comparison between different accounting policies that management choose to make (for example, one entity may amortise customer lists over 10 years, whereas another entity may decide to amortise customer lists over 20 years). They think that information provided by intangible assets is more useful than information provided by goodwill.

(d) all intangible assets wear out and the amortisation reflects the need for future investment to replace them, in addition to the expensed ‘maintenance’ costs of marketing, research etc.

What are the main implementation, auditing or enforcement challenges in the separate recognition of intangible assets from goodwill? What do you think are the main causes of those challenges?

45. Many participants[44] think that some intangible assets, such as internally generated brands and customer lists, are difficult to distinguish from the business as a whole and could require subjective and arbitrary allocation of future cash flows among these intangible assets and other assets.

46. The main causes of the challenges in recognising and measuring intangible assets described by participants are:

[44] See, for example, ASC’s comment letter.

(a) many intangible assets are not frequently traded on a stand-alone basis and therefore very often there is no active market for them;

(b) many intangible assets are unique and therefore not easy to identify and assess their value;

(c) valuation methods are complex and subjective;

(d) values may be attributed to the wrong asset due to confusion on the source of profit generation;

(e) the measurement is more complex/subjective when the intangible assets are not based on legally enforceable rights;

(f) the lack of any thresholds in terms of control or measurement reliability means that some respondents assert that this requires a search for intangible assets to recognise separately at a very granular level—these respondents also say that the measurement of these intangibles are also highly judgemental;

(g) the acquirer already owns the intangible assets (for example, customer relationships when there is an overlap in the customer base of the acquirer and the acquiree);

(h) the acquirer does not intend to use the intangible assets (for example, a brand acquired and held for defensive reasons); and

(i) the useful life of some intangible assets is subjective.

47. According to the report[45] published by ESMA in June 2014:

(a) 77 per cent of the issuers included in the sample recognised intangible assets other than goodwill as part of the business combination.

(b) 54 per cent of the total amount of intangibles (including goodwill) related to separable intangible assets.

(c) intangible assets for which usually there is no observable market, such as customer-related and marketing-related intangibles, were the most common assets recognised in the review. The customer- related

45 ESMA Report: *Review on the application of accounting requirements for business combinations in IFRS financial statements*.

intangibles included customer relationships, customer lists, customer contracts and order backlogs. Marketing-related intangibles mainly related to brand names and internet domains.

(d) techniques used to measure fair values in a business combination vary significantly and often external experts are engaged.

(e) ESMA noted that the most prevalent intangible asset recognised separately from goodwill related to customer relationships. Customer relationships stem from both contractual and non-contractual relationships. In its *Update* from March 2009, the IFRS Interpretations Committee (the 'Interpretations Committee') dealt with a question on the circumstances in which a non-contractual customer relationship arises in a business combination and concluded that the way that a relationship was established helps to identify whether a customer relationship exists but should not be the primary basis for determining whether the acquirer recognises an intangible asset. Due to the widespread diversity observed by the Interpretations Committee, it decided to refer this question to the IASB. ESMA's experience and the review results confirm that customer relationships play a significant role in business combinations, thus ESMA encourages the IASB to work on this topic as part of the PIR and, in particular, to deal with the recommendation from the March 2009 Interpretations Committee decision.

How useful do you find the recognition of negative goodwill in profit or loss and the disclosures about the underlying reasons why the transaction resulted in a gain?

48. Users usually strip out gains from bargain purchases from their assessment of underlying earnings. Many users think that such gains are not part of the performance of the company. Many users have no strong views on the accounting treatment of negative goodwill. They are not significantly concerned about the current accounting for negative goodwill, as long as the amount of the gain is clearly disclosed in the financial statements or in the notes. Other users think that

recognising gains from bargain purchases in other comprehensive income (OCI) would be a better option.

49. Users usually find the disclosures required by IFRS 3 about negative goodwill useful, because if an entity recognises negative goodwill, then it is important to know why the transaction resulted in a bargain purchase.

50. Some users[46] tend to assume that the transaction price is the fair value on that date. In their view, if it is genuinely a bargain, the benefits will come through in subsequent profits and revaluations.

51. Some users[47] think that the recognition of negative goodwill in the profit and loss does not help them in understanding how well a business is managed or the future prospects for that business.

52. Some users[48] would like to limit the recognition of a bargain purchase gain to those cases in which the fair values can be ascertained by prices set in active markets.

53. Some participants[49] note that negative goodwill arises more frequently in practice than was indicated in the Standard. They observe that negative goodwill arises in a number of different circumstances, such as where:

    (a) companies are sold during periods of distress (for example, during the recent financial crisis);

    (b) restructuring provisions are required and contemplated in the economics of a deal but cannot be recorded at acquisition under the Standard; or

    (c) share prices fluctuate significantly subsequent to fixing the exchange ratio.

54. According to the report published by ESMA in June 2014:

    (a) business combinations accounted for as bargain purchases are not rare. A bargain purchase gain was reported in 11 per cent of the business combinations reviewed. The gains ranged between 1 per cent and 130

[46] See, for example, CFA UK's comment letter.

[47] See, for example, Enderson Global Investors' comment letter.

[48] See, for example, EFFAS's comment letter.

[49] See, for example, PWC's comment letter.

per cent of the consideration paid for the acquisition and between 1 per cent and 32 per cent of the net income before tax of the acquirer. On average, the bargain purchase gains represented around 46 per cent of the consideration paid and around 12 per cent of the net result before taxes.

(b) in some situations bargain gains result because future restructuring costs that cannot be recognised, despite the fact that they were considered in the negotiations when determining the purchase price of the acquisition or they were deemed necessary.

Non-amortisation of goodwill and indefinite-life intangible assets

How useful have you found the information obtained from annually assessing goodwill and intangible assets with indefinite useful lives for impairment, and why?

55. Some users supported the current requirements on subsequent measurement of goodwill and indefinite-lived intangible assets, because they think that the non-amortisation of goodwill:

(a) is useful for relating the price paid to what was acquired and for calculating the Return on Invested capital (ie RoI).

(b) helps them to assess the stewardship of the management. It gives them a better understanding of whether the management has overpaid or whether the acquisition was successful.

(c) helps them to verify whether an acquisition is working as expected and whether the acquirer is still expecting future economic benefits, such as synergies, from the business combination.

(d) impairment test of goodwill can act as a clearing event, which demonstrates to investors that management has recognised previous mistakes and can ‘move on’.

They consider the amortisation of goodwill to be only an arbitrary allocation exercise (ie it does not provide useful information). Consequently, they would disregard the amortisation of goodwill in their analysis.

56. They think that the information provided by the impairment test of goodwill is useful, because it has a confirmative value. However, they admit that impairment losses are often recognised too late (ie it has not predictive value).

57. Other users supported the amortisation of goodwill and indefinite-lived intangible assets, because they think that:

(a) assumptions used in the impairment test are too optimistic and difficult to analyse.

(b) impairment losses are recognised when the investors have already reached a view that the company over paid for the acquisition and, therefore, the market ignores the impairment test results (ie the impairment loss is already included in the share price).

(c) estimating the useful life of goodwill is possible and is no more difficult than estimating the useful life of other intangible assets.

(d) goodwill has been paid for and so, sooner or later, it should have an impact on profit or loss.

(e) goodwill represents future profits, thus should be allocated over time.

(f) amortising goodwill reflects that the acquirer need to 'maintain' the profitability of the acquired company. The amortisation reflects the costs incurred by acquirer to maintain such profitability.

(g) amortising goodwill would decrease volatility in profit or loss when compared to an impairment model.

(h) amortising goodwill would improve comparability between companies that grow organically (ie without acquisitions) and companies that grow through acquisitions, because the non-amortisation of goodwill discriminates companies that grow organically.

(i) goodwill acquired in a business combination is supported and replaced by internally generated goodwill over time.

(j) amortising goodwill would reduce pressure on the identification of intangible assets, because both goodwill and intangible assets would be amortised.

58. Many users think that information required by IAS 36 *Impairment of Assets* is useful. Useful disclosures include discount rates used, long-term growth rates, profit and capital expenditure assumptions and sensitivities. However, some users think that the disclosed information is boilerplate and insufficient for them to assess whether or not the main inputs/assumptions are reasonable.

59. Some participants[50] suggest an amortisation and impairment approach. They think that the reintroduction of amortisation of goodwill:

(a) would be appropriate, because it reasonably reflects the consumption of the economic resource acquired in the business combination over time, and can be applied in a way that achieves an adequate level of verifiability and reliability; and

(b) does not replace the need for a robust impairment model.

60. Similarly, some participants[51] suggest that goodwill should be amortised over the period and to the extent that the profits were expected to arise from the business combination at the acquisition date. Subsequent changes to the original business plan should not be reflected in the amortisation pattern. Due to the time value of money and the uncertainty inherent in the estimation of future profits, they would expect that the amortisation charge of goodwill would decline over time. Under this model, an impairment test would only need to be performed if specific impairment indicators would arise. They think that such a treatment would better reflect the economic substance of a business combination in the following years as well as eliminate the current accounting discrepancy between internally generated and acquired goodwill. As an additional benefit, this model would be less complex and less costly, as no annual impairment test would need to be performed unless there are specific impairment indicators.

61. Similarly, according to a report[52] published by KPMG in April 2014:

(a) the high number of judgements and assumptions make the goodwill impairment testing a complex and time-consuming exercise;

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[50] See, for example, the Discussion Paper *Should goodwill still not be amortised?*, which was published by ASBJ, EFRAG and OIC in July 2014.

[51] See, for example, SIX Swiss Exchange's comment letter.

[52] See the report *Who cares about goodwill impairment?*

(b) it is not clear that the benefits of mandatory annual impairment testing outweigh the related costs;

(c) the value relevance of impairment testing is in confirming instead of predicting value, and that goodwill impairment charges do not act as a major signalling event for the market; and

(d) there is considerable support for a return to an amortisation-based model of accounting for goodwill with indicator-based impairment testing.

Do you think that improvements are needed regarding the information provided by the impairment test? If so, what are they?

62. Many participants think that the information provided by the impairment test as well as the related disclosures requirements is comprehensive.

63. Some users[53] think that to make impairment tests more useful, companies should carry them out whenever there is a significant change in market conditions that would drive a change in profit forecasts. In their view, the need to conduct a test in response to value-threatening events should be reinforced. They also think that more information about the assumptions fed into valuation models would be useful. Such granular disclosure should come out as soon as possible (ie with the preliminary full-year results, instead of just appearing in the notes of the annual report).

64. Some participants[54] suggest the following possible improvements:

(a) requiring mandatory disclosure of the sensitivity analysis.

(b) clarify that when a sensitivity analysis needs to be provided, the requirement does not only apply to the growth rate and the discount rate but also to other key assumptions.

(c) in the light of the fact that post-tax rate is used when calculating fair value according to IFRS 13 *Fair Value Measurement*, the requirement to disclose only the pre-tax rate when measuring the recoverable amount based on the value in use calculation should be reconsidered.

[53] See, for example, CFA UK's comment letter.

[54] See, for example, ESMA's comment letter.

Use and disclosure of the pre-tax rate for the goodwill impairment test can be confusing to users of financial statements, because observable market information is available only for post-tax rates.

What are the main implementation, auditing or enforcement challenges in testing goodwill or intangible assets with indefinite useful lives for impairment, and why?

65. Many participants think that the impairment test is complex, time-consuming and expensive and involves significant judgements. The main challenges identified are the following:

(a) determining the cash flows from the cash generating unit to which the goodwill has been allocated, the discount factor to be applied and the terminal value (growth rate) of the cash flows can be very judgemental. Cash flows projections must be prepared specifically for the purpose of impairment testing, as management projections are not based on an 'as is' status, but also include management best estimates of future cash flows derived from new investments and products.

(b) the allocation of goodwill to cash generating units (CGUs) for impairment testing. Goodwill is allocated to the CGUs that are expected to benefit from the synergies of the combination, which can be judgemental and difficult to apply in practice. After the initial allocation, the carrying value of the goodwill is tested for impairment as part of the respective GCUs, which might be merged or restructured in subsequent years to a degree that they have little or no similarities to the originally acquired business. Furthermore, the impairment test is performed based on the most recent approved budgets, which over time can be substantially different from the business plans at the acquisition date.

(c) it is not clear what represents 'the lowest level within the entity at which the goodwill is monitored for internal management purposes', as set out in paragraph 80 of IAS 36.

(d) practical difficulties related to the testing of a CGU for impairment when part of the recoverable amount is attributable to non-controlling interest (NCI). If an entity is measuring NCI at its proportionate share of net assets, this needs to be reflected in the impairment calculation. This becomes more complicated when there have been transactions with NCI holders after the business acquisition date, or if there is a group of CGUs to which goodwill is attributed that is partly measured at fair value and partly on a proportionate basis.

(e) the requirement to use a pre-tax discount rate when equity returns are always post-tax (meaning there are not observable market inputs for a pre-tax cost of equity). Practically, this means that the test is usually conducted on a post-tax basis with an additional iteration performed simply to derive a pre-tax discount rate.

(f) separating forecast capital expenditures between maintenance capital expenditures and expansionary capital expenditures; particularly, how this separation impacts subsequent cash flows, not just the exclusion of expansionary capital expenditures itself.

Non-controlling interests

How useful is the information resulting from the presentation and measurement requirements for NCIs? Does the information resulting from those requirements reflect the claims on consolidated equity that are not attributable to the parent? If not, what improvements do you think are needed?

66. Most users support the presentation requirements for NCIs. However, some users would prefer presentation of NCI within debt or between debt and equity because they do not see how NCIs represent shareholders' equity.

67. Many users do not support the measurement choice for NCIs between fair value and proportionate share in the recognised amounts of the acquiree's identifiable net assets. However, they provided mixed views on how an entity should measure NCIs. Some prefer the proportionate method, others prefer the fair value method and others did not have a preference. Many of them are opposed to having options, particularly on a case-by-case basis because it makes it difficult to compare companies that account for partial acquisitions differently.

68. Many users think that it is important to know the reason why an entity has chosen one of the measurement options.

69. Some users[55] think that the revision of the Standard that requires recognising goodwill only at the acquisition date is inconsistent with what investors wants to follow, ie capital invested. For example, if we assume that a group acquires control with 51 per cent of the capital for CU1,000 and, 10 years later, while the acquired business has developed very successfully, the 49 per cent is bought out for CU3,000; in the consolidated financial statements, the amount of capital invested in the subsidiary would remain unchanged despite the very significant additional investment. They also stress that this approach has very disturbing consequences (that were identified when the Standard was revised). In the above example, after buying the NCI in a very successful business, the group will most probably report a significant decrease in the parent company equity: consequently, making a good investment significantly reduces equity. They also think that the choice made by numerous companies to use full goodwill, instead of the partial goodwill, is due to the fact that the latter option might lead to reducing more equity at a later stage should the non-controlling interests be bought out.

70. Some users prefer that companies should be required to measure NCIs at fair value, because when valuing a company analysts will seek to determine a market price for NCIs.[56]

71. Some participants[57] think that while the measurement of NCI at fair value may be more consistent conceptually with the entity perspective in IFRS 3 and IFRS 10 *Consolidated Financial Statements*, the subjectivity involved in this measurement is such that the information produced is not necessarily more relevant than a measurement based on net identifiable assets.

[55] See, for example SFAF's comment letter.

[56] See, for example CFA UK's comment letter.

[57] See, for example DT's comment letter.

What are the main challenges in the accounting for NCIs, or auditing or enforcing such accounting? Please specify the measurement option under which those challenges arise.

72. Most of the participants that expressed a view on this issue measure NCI at the proportionate share in the recognised amounts of the acquiree's identifiable net assets.

73. Many participants think that measuring NCI at fair value presents significant practical difficulties, in particular when the shares of the acquiree are not traded in an active market. They note that the acquisition of a majority shareholding includes a control premium that should not be considered in the value of the NCI and that there is no objective way to determine this control premium.

74. Some participants[58] think that there are still problems arising in practice in dealing with put options over NCIs and request that the IASB restarts its work in this area. They also think that the issue of accounting for mandatory tender offers should be addressed.

75. Some participants[59] note that in a subsequent sale of interests to NCI while retaining control, IFRS 10 requires the NCI to be adjusted. However, in their view, it is not clear how this adjustment should be made, especially when an entity elected to measure NCI using the proportionate interest approach. One approach is to base the change on subsidiary equity (net assets) but this means that the re-allocation deduction includes an element of goodwill whereas the initial measurement did not. In an extreme case, this can lead to a negative balance of NCI. An alternative approach is to base the change on a proportion of the reported NCI balance, with or without an analysis of whether the underlying transactions that gave rise to the NCI includes an element of goodwill.

76. Some participants[60] think that the basis of measurement of NCI has consequences on the subsequent impairment test on goodwill. The following issues have been identified:

    (a) NCI at fair value: IAS 36 indicates that if a subsidiary, or part of a subsidiary, with a NCI is itself a cash-generating unit, the impairment

[58] See, for example, FEE's comment letter.

[59] See, for example, KPMG's comment letter.

[60] See, for example, DT's comment letter,

loss is allocated between the parent and the NCI on the same basis as that on which profit or loss is allocated. Accordingly, despite the fact that the goodwill attributable to the parent and to the NCI may not be proportional to the percentage of ownership held by each, any impairment loss arising on the goodwill shall be allocated to the parent and to the NCI on the same basis as that on which profit or loss is allocated (ie in proportion to their respective present ownership interests).

(b) NCI at a proportionate share of net asset: it may be useful to clarify whether the gross up of goodwill required by IAS 36 can be made on a basis other than proportionally and, if so, in what circumstances can an alternative basis be used.

Step acquisitions and loss of control

How useful do you find the information resulting from the step acquisition guidance in IFRS 3? If any of the information is unhelpful, please explain why.

77. Many users think that the gain or loss on the remeasurement at fair value of the previously held interest is a non-recurring gain or loss that is not part of the performance of the entity. Consequently, such gains (or losses) are not considered in their valuation models. For this reason, many users think that it would be useful to have these gains (or losses) clearly identified in the financial statements. Some of them suggest recognising the gain or loss on the remeasurement of the previously held equity interest in OCI.

78. Some users say that the previously held equity interest should not be remeasured at the acquisition-date fair value, because they think that:

(a) the fair value of the previously held interest does not give better information about future cash flows than a carry-over basis. The cost paid for each stake is useful to assess management stewardship.

(b) the current requirements produce counterintuitive results, because the more that the acquirer pays, the bigger the gain that it recognises in its profit or loss.

(c) the unit price for a large block of shares is different from the unit price for the last few shares needed to acquire control. A previously held large minority interest should not be remeasured at the price paid to acquiring the last few shares that were publicly traded.

(d) the earning process is not complete and the gain has not been realised.

How useful do you find the information resulting from the accounting for a parent's retained investment upon the loss of control in a former subsidiary? If any of the information is unhelpful, please explain why.

79. Similarly as for step acquisitions, many users think that the gain or loss on the remeasurement at fair value of the retained interest in the former subsidiary is a non-recurring gain or loss that is not part of the performance of the entity. Consequently, they think that it would be useful to have these gains (or losses) clearly identified in the financial statements. Some of them suggest recognising these gains or losses in OCI.

80. Some users think that the gain on the remeasurement of the retained equity interest should not be recognised in profit or loss, because the earning process is not complete and the gain has not been realised. They consider this gain as an hypothetical gain, because there is no cash flow.

Disclosures

Is other information needed to properly understand the effect of the acquisition on a group? If so, what information is needed and why would it be useful?

81. Many users think that once an acquisition has been completed it is often hard to track the subsequent performance of the acquired business. Consequently, they think that better disclosure is needed to allow them to do so. For example, it is important for them to know how much of the business has grown organically versus how much it has grown through acquisitions. Up to the end of the first full year after the acquisition, it would be helpful for them to know the contribution of the acquiree to revenue, gross profit and/or operating profit.

82. Many users also require clear information on the operating performance of the acquired business, specifically, revenue and operating profit over preceding

periods and pro-forma prior year comparative information for the combined entity for purposes of their trend analysis.

83. Users often seek to assess the return on the capital (cash or cash equivalent) that has been deployed in an acquisition. However, they think that it is often difficult to ascertain what consideration has been paid for an acquisition. For them it is critical to calculate the total consideration including cash paid, cash acquired, debts and pensions liabilities assumed, fees and restructuring costs, shares and notes issued to the vendor together with any deferred consideration. They told us that:

    (a) beyond the cash paid and cash acquired, disclosure is often incomplete; and

    (b) entities are required to provide information on the major categories of assets and liabilities acquired but short term debt, for instance, can be ‘hidden’ within current liabilities.

84. They also think that it would be useful also to have more information about the inputs and methodologies used to measure the fair value of the acquired assets and liabilities, such as the disclosures in IFRS 13.

85. When there are anticipated restructuring costs in order to realise the synergies that justify an acquisition, some users would like the company to disclose subsequent progress (amounts and timing) on achieving the cost savings and on the related spending on restructuring. They also think that, since tax arbitrage is increasingly being cited as a potential ‘benefit’ of an acquisition, the acquirer should set out its targets for tax rate reduction and the potential gains to net income. Post-acquisition, progress on achieving these gains should be reported on along with the gains from restructuring etc.

86. Some users would like to see a requirement to disclose the acquiree's carrying amount of the assets acquired and the liabilities assumed by the acquirer at the acquisition date and any fair value adjustments to these amounts. They think that knowing which types of assets had significant increases in fair value over the carrying amount in the acquiree's financial statements would be useful to them in evaluating the post-acquisition statement of financial position.

87. Many users expressed concerns about the quality of the information disclosed about the primary reasons for business combinations. In their view, entities often

provide very general 'boiler plate' explanations that lacked insight on the real economic reasons for the acquisition.

88. Some users ask the IASB to improve IAS 34 with regards to information on business combinations. They think that this information is less comprehensive than information reported in annual financial statements and that the timing of disclosures is crucial, given stock prices sensitiveness to companies' business combinations announcements. In addition, in their view, the interim financial statements do not sufficiently explain the developments in business combinations that are still within the measurement period under IFRS 3.

89. Some users note that, in some cases, preparers present the disclosures in a number of different notes to the financial statements, which may make it difficult to fully understand the impact of the acquisition. Requiring all of the relevant disclosures to be presented in one place may be useful.

90. Some users would like more information about:

(a) the nature of the intangible assets that are recognised as a result of a business combination; and

(b) the underlying criteria and rationale used by management when identifying and separating intangibles from goodwill.

Is there information required to be disclosed that is not useful and that should not be required? Please explain why.

91. Many participants find it very difficult to disclose the revenue and profit or loss of the combined entity for the current period as though the acquisition had occurred at the beginning of the reporting period, because information prior to the acquisition is not always readily available. Due to the practical limitations and the significant effort required to determine the disclosures, they think that the IASB should consider providing some relief from this disclosure requirement.

92. Some participants[61] think that:

(a) the requirement to provide disclosure about the impact of acquisitions made after the reporting date, but before the financial statements are

[61] See, for example, EY's comment letter.

authorised, can be difficult, because the information is not often known and so the disclosures are not always meaningful; and

(b) the disclosures made regarding the qualitative description of goodwill are often generic and tend not to provide useful information.

93. Some participants[62] question whether the information required by paragraph B64(h) of IFRS 3 is useful for the users. The paragraph requires disclosing fair value, the gross contractual amount and the best estimate of collection for all classes of receivables. In their view, such detailed information should only be required if it is important for understanding the business acquired. Moreover, if such detailed information is important, the disclosure requirement should apply to any acquired asset or liability, not only receivables.

What are the main challenges to preparing, auditing or enforcing the disclosures required by IFRS 3 or by the related amendments, and why?

94. Similarly as for the previous question, many participants think that the pro-forma information relating to the revenue and profit or loss of the combined entity for the current period as though the acquisition had occurred at the beginning of the reporting period is difficult to prepare and consequently to audit. Some participants[63] think that if users indicate that this pro-forma information is useful, the IASB should consider whether further guidance is required. For example, what adjustments, if any, should be made in combining the results of the acquirer and the acquiree for the period before the acquisition?

95. According to the ACCA Research Report *Worldwide application of IFRS 3, IAS 38 and IAS 36, related disclosures, and determinants of non-compliance*:

(a) although 258 companies disclose that they recognise goodwill, only 61 disclose a qualitative description of the factors that make up this goodwill. This leads to the conclusion that a large number of companies fall short of the IFRS 3 requirement for such information. In most cases, even the 61 companies that do provide a description give nothing

[62] See, for example, NASB's comment letter.

[63] See, for example, DT's comment letter.

more than a brief statement referring to synergies expected to arise from the combinations.

(b) out of the 76 companies for which acquisitions involve between 50 per cent and 99 per cent of the acquiree's assets, 33 remain silent on how the non-controlling interest is measured. Additionally, only 11 companies (14.4 per cent) explicitly state that they measure their non-controlling interest at fair value (full goodwill approach), indicating that the newly introduced alternative method is not popular among firms.

(c) on average, 38.9 per cent of the total purchase price is allocated to 'other intangible assets'. Companies are not explicit on what is recognised in this 'class' of assets so there is a need for supportive disclosures on what these assets constitute.

A large number of the sample companies do not disclose pro-forma information about the business combinations.

Other matters

Are there other matters that you think the IASB should be aware of as it considers the PiR of IFRS 3?

96. Many participants think that the IASB should reconsider the subsequent accounting for contingent consideration. We report below an abstract of the EFRAG comment letter:

> Several preparers expressed concern about the measurement of contingent consideration particularly when it was based on technical accomplishments or future business achievements (especially for early stage or transactions with multiple targets). It was challenging to fair value these future contingent payments at the acquisition date based on the probability of success of each milestone.
>
> Some preparers noted that when contingent consideration liabilities are directly linked to a particular (new) intangible asset acquired (for example an in-process research project), the values of the liability and related intangible asset respond equally to the related changes in the

> development of the project. These preparers suggest that changes in fair value of the liability could be recognised as an adjustment to the related intangible asset, instead of in profit or loss, to avoid potential “accounting mismatches”.
>
> Most users thought that contingent consideration should be part of acquisition price for the business combination and therefore added to the investment value. . These users did not think that gains and losses resulting from future price adjustments were part of the performance of a company. Users generally indicated that it was important to understand the factors that led to “postponed” consideration payments, and less concerned “where in the accounts” the adjustments were recognised as they would exclude them from the performance statement. The structure of consideration package, including contingent consideration, and its effects on the company’s debt structure, was considered by some users as vital information.

97. Many participants ask the IASB to revisit the guidance in paragraph B55(a) of IFRS 3, for contingent payments to selling shareholders in circumstances in which those selling shareholders become, or continue as, employees. They note that the paragraph appears to mandate that an arrangement in which contingent payments are forfeited if employment terminates is treated as post-acquisition remuneration. In their view, this should not be an individually conclusive rule, but one of the indicators that should be considered in assessing whether such contingent consideration should be treated as part of the consideration transferred in the acquisition or as a post-acquisition expense.

98. Some participants[64] express concerns regarding the application of measurement requirements in IFRS 3 to determine whether pre-existing relationships are favourable or unfavourable. They note that the determination can be very burdensome and involves, in most cases, a significant degree of management judgement. There are also concerns regarding the accounting implications for the settlement of pre-existing relationships through business combinations. Beside the concerns about recognising gains in profit or loss when no effective realisation of such gain has occurred, concerns relate to the fact that the judgement to determine whether pre-existing relationships are favourable or unfavourable impacts the determination of acquired goodwill.

[64] See, for example, ASCG’s comment letter.

99. Some participants[65] argue that transaction costs involved in a business combination should be included in the cost of the business combination, because the current accounting treatment (ie they are expensed) is inconsistent with other asset acquisitions.

100. Some participants[66] think that the recognition of restructuring provisions/expenses after the acquisition date, when these expenses were identified and taken into account in the transaction as a whole, is not considered to be providing useful information. This is especially the case when a negative goodwill is recognised.

101. Many respondents ask the IASB to provide guidance on business combinations under common control and appreciate that the IASB currently has a research project on this matter.

Effects

Which areas of IFRS 3 and related amendments represent benefits to users of financial statements, preparers, auditors and/or enforcers of financial information, and why?

102. The main benefits respondents say they see are:

(a) IFRS 3 and the related amendments provide an appropriate and coherent framework for accounting for business combinations that is converged with US GAAP;

(b) the information derived from fair value measurements in a business combination is valuable for users and as such can serve to explain management's intention behind the takeover;

(c) the approach of clearly setting out the Standard's principles and then highlighting exceptions to them generally makes it easy to follow and understand;

(d) enhanced transparency due to the extensive disclosures;

[65] See, for example, GLASS's comment letter.

[66] See, for example, ANC's comment letter.

(e) the identification of intangibles apart from goodwill provides users with critical information on the underlying fundamental drivers of value in businesses that a management team is choosing to invest in.

Which areas of IFRS 3 and related amendments have resulted in considerable unexpected costs to users of financial statements, preparers, auditors and/or enforcers of financial information, and why?

103. Many respondents think that the most considerable unexpected costs arise from the fair value measurement, separation of intangible assets from goodwill and the impairment test, because these areas of IFRS 3 sometimes require the involvement of external valuation specialists.

Which areas of IFRS 3 and related amendments have had an effect on how acquisitions are carried out (for example, an effect on contractual terms)?

104. Many participants are not aware of any changes to the way acquisitions are carried out or structured. However, some had the following perceptions:

(a) entities could overestimate contingent consideration to avoid negative effects in the post-acquisition profit or loss;

(b) entities try to avoid contingent consideration when possible; and

(c) the increased alignment between US GAAP and IFRS makes deal negotiations and structuring between different parts of the world more straightforward.

Staff recommendation and next steps

105. In our view, we have received enough information to prepare a Feedback Statement, including staff recommendations of areas for which agenda proposals should be prepared. We intend to bring these to the IASB for discussion at a subsequent meeting.

Questions to the IASB
1. Do you agree that we have enough information to prepare a Feedback Statement for your review?

2. Do you have any comments to add to the comments and messages contained in this paper?

Appendix A - Overview of the comment letter respondents and outreach conducted

Comment letter respondents

A1. The RFI was issued on 30 January 2014 and the comment letter period ended on 30 May 2014. The IASB received 93 comment letters, which are summarised below by type of respondent and geographical region.

Type of comment letter respondent

Type of respondent	Number of respondents	Percentage of respondents
Preparers and industry organisations	38	41%
Accounting firms and accountancy bodies	21	23%
Standard-setters	14	15%
Investors	4	4%
Regulators and government agencies	6	6%
Academia	4	4%
Other	6	6%
Total	**93**	**100%**

A2. A diverse range of types of interested parties responded to the RFI.

A3. The responses from investors are limited as is often the case when dealing with a formal comment letter process. However, it should be noted that:

a. 3 out of the 4 investors that replied to the RFI are representative bodies and therefore reflect the views of more than one entity or individual;

b. many responses from standard setters include investors' views;

c. we heard from several investors and investors representative bodies through outreach activities (see Appendix B to this paper).

Geographical distribution of comment letter respondents

Geographical region	Number of respondents	Percentage of respondents
Europe	45	48%
Asia and Oceania	21	16%
International	7	8%
Americas	14	15%
Africa	3	3%
Not specified	3	3%
Total	**93**	**100%**

A4. All geographical regions are represented in the responses. Europe is the geographical region providing most respondents, reflecting that region's early adoption of IFRSs compared with other, more recent, adopters of IFRSs.

Overview of outreach conducted

A5. Throughout the first half of 2014, members and staff of the IASB took part in many outreach activities to raise awareness of the post-implementation review process across all interested parties and to collect information about the effect of implementing IFRS 3.

A6. In addition, many national standard-setters and regional forums undertook a number of local initiatives to widen the range of consultation.

A7. In this information-gathering phase, the members of the IASB and staff took part in 30 outreach events, which are summarised below by type of participant and geographical region.

Type of participants and outreach activities

Participant type	**Number of events**	**%**
Preparers	4	13%
Investors and Investors representative bodies	19	63%
Mixed groups (ie regulators, auditors, preparers and users)	7	23%
Total	**30**	**100%**

A8. A number of formats were employed for this outreach, including roundtables, discussion forums, videoconferences and one-to-one interviews.

A9. We focused our outreach activities on investors and investors representative bodies, because:

a. we expected few comment letters from investors; and

b. many questions included in the RFI aim to get investors views on such questions.

A10. We attended a number of public discussion forums organised by local or regional standard-setters, regulators or other institutions. These forums generally included a cross-section of all types of participants, including preparers, users, regulators and accounting firms.

Geographical distribution of outreach conducted

Geographical region	Number of events	Percentage of events
Europe	20	67%
Asia and Oceania	3	10%
International	4	13%
America	2	7%
Africa	1	3%
Total	**30**	**100%**

A11. All geographical regions were represented in the outreach conducted. The geographical distribution of outreach conducted shows similar characteristics to that for comment letter respondents that is discussed in paragraph AA4 of this Appendix.