STAFF PAPER

June 2016

IASB/FASB Meeting

Project	**Goodwill and impairment project**
Paper topic	Progress report: Goodwill and other intangible assets in a business combination

CONTACT(S)	Michelle Fisher	mfisher@ifrs.org	+44(0)20 7246 6918

Objective of this paper

1. The goodwill and impairment project is expected to run in two concurrent phases—a goodwill and other intangible assets phase and an impairment phase.[1] The purpose of this agenda paper is to provide an update on our progress in the goodwill and other intangible assets phase of this project.

Structure of this paper

2. This paper includes the following sections:
   (a) Update since September 2015 meeting with the US Financial Accounting Standards Board (FASB)
   (b) Objective of looking at goodwill and other intangible assets acquired in a business combination
   (c) Summary of approaches being considered
   (d) Staff observations and proposed next steps

[1] At previous Board meetings we have discussed having two separate phases. This is because the topics 'subsequent accounting for goodwill' and 'identification of intangible assets separately from goodwill' are expected to be considered with the US FASB to maintain convergence. Improvements to the impairment requirements are expected to be Board only discussions, at least initially.

(e) Appendix A: Feedback from the Post-implementation Review (PIR) of IFRS 3 *Business Combinations* on subsequent accounting for goodwill

(f) Appendix B: Feedback from the IFRS 3 PIR on identification and measurement of other intangible assets acquired in a business combination

(g) Appendix C: Staff analysis of guidance for customer-related intangible assets.

(h) Appendix D: IFRIC[2] agenda decision in March 2009 IFRIC update newsletter

Update since September 2015 meeting with the FASB

3. The Board discussed subsequent accounting for goodwill at its October 2015 and February 2016 meetings. The Board discussed identification and measurement of other intangible assets in a business combination (ie intangible assets other than goodwill) at its November 2015 and February-March 2016 meetings. The following were discussed and developed:

   (a) The objectives for this phase of the project (see paragraphs 7-8)

   (b) Possible approaches to addressing the objectives. These are described in paragraphs 9-18.

   The meetings were not decision-making meetings.

4. At the November 2015 meeting of the Capital Markets Advisory Committee (CMAC) the staff asked for CMAC members' views on goodwill amortisation and how they currently use the information provided by entities about goodwill and impairment.

5. At the December 2015 meeting of the Accounting Standards Advisory Forum (ASAF), the staff asked for feedback on the Board's initial discussions in October and November 2015 and for advice on the way forward with the project.

6. At the May 2016 Board meeting, staff from the Accounting Standards Board of Japan (ASBJ) and the European Financial Reporting Advisory Group (EFRAG) presented their data research, which includes quantitative information from 2007 to 2014 about

[2] The IFRS Interpretations Committee was previously called the IFRIC.

the amounts and trends of reported goodwill, impairment and intangible assets in four major indices in the US, Europe, Australia and Japan. The staff think the following were the main points from that research:[3]

(a) The absolute amounts of both goodwill and other intangible assets have generally increased over the period.

(b) The ratios 'goodwill/net assets' and 'intangible assets (including goodwill)/net assets' have generally declined slightly over the period.

(c) The ratios 'goodwill/market capitalisation' and 'intangible assets (including goodwill)/market capitalisation' have been volatile during the period, reflecting the volatility in share prices during the period. However, the 2007 and 2014 ratios are similar values.

(d) An unsophisticated calculation shows that it would take between 5-72 years at the current rate of impairment (plus amortisation in Japan) for the total goodwill balance to be written off.[4]

(e) There are significant variations in the data across different industries.

Objective of looking at goodwill and other intangible assets acquired in a business combination

7. The main objective of looking at subsequent accounting for goodwill is to consider whether and how the costs of the current accounting can be reduced without a reduction in quality of information for investors.

8. The main objective of looking at identification and measurement of intangible assets is to consider whether there are cost benefit reasons to subsume within goodwill any identifiable intangible assets acquired in a business combination. This review includes

[3] Agenda Papers 18B and 18C for the May 2016 Board meeting presented the detailed research of the ASBJ/EFRAG staff.

[4] The unsophisticated calculation was as follows. For a given market index, the ratio 'total goodwill at the start of the year/total goodwill impairment charge during the year (plus amortisation in Japan)' was calculated. This was intended to give a basic measure how long it would take to write off the current goodwill balance at the current rate of impairment. Based solely on data for 2014, and presented in May 2016 Agenda Paper 18B, this ratio ranged from 130 years in the US to 11 in Japan (where amortisation is required). When calculating an average over the period 2007-2014 the ratio reduced to a range of 5-72 years.

considering whether guidance or education material would help mitigate cost benefit concerns without changing the requirements.

Summary of approaches being considered

Possible approaches for subsequent accounting for goodwill

Discussed at October 2015 and February 2016 Board meetings[5]

Approach G1 An amortisation and impairment model

9. Amortise goodwill over its expected life with impairment testing, with guidance on determining an appropriate useful life and amortisation method. The following sub issues would likely need to be addressed under this model:

   (a) how the useful life of goodwill should be determined;

   (b) whether there should be an upper limit on that useful life;

   (c) how the amortisation method should be determined;

   (d) whether annual reassessment of the amortisation method and useful life should be required;

   (e) whether other intangible assets can have an indefinite life or whether all intangible assets should be amortised;

   (f) allocation of impairment to amortisable units of goodwill when a cash-generating unit (CGU) contains goodwill arising from different acquisitions; and

   (g) allocation of goodwill to amortisable units of goodwill on a disposal or reorganisation.

Approach G2 Direct write off of goodwill

10. Write off goodwill on acquisition. Possible approaches for recognising the write off:

   (a) as an expense in profit or loss; or

[5] The detailed staff analysis of these approaches is in February 2016 Agenda Paper 18B and October 2015 Agenda Paper 18A.

(b) as an expense in other comprehensive income (OCI) or direct recognition in equity (with or without 'recycling' on subsequent disposal or impairment).

11. We could also consider variants of this method:

    (a) if there should be a rebuttable presumption that goodwill should be written off unless the entity can demonstrate that the goodwill is an asset.

    (b) if some component of goodwill (for example representing a genuine overpayment or overvaluation) could be separated from the rest of goodwill and written off.

Approach G3 Impairment only model

12. No changes to the current accounting for goodwill, other than any improvements made to the impairment requirements in IAS 36 (see Agenda Paper 18B for this meeting).[6]

Possible approaches for other intangible assets in a business combination

Discussed at November 2015, and February-March 2016 Board meetings[7]

Approach T1 No change

13. No change to existing requirements, and hence no change to the composition of goodwill. Consider improving the guidance in IFRS 3/IAS 38 for those intangible assets that feedback suggests are difficult to identify and measure, for example customer relationship intangible assets (some ideas are suggested in Appendix C).

Approach T2 Subsume some intangible assets in goodwill

14. Subsume some identifiable intangible assets in goodwill for cost-benefit reasons. Possibilities to consider are:

    (a) The main intangible assets for which we have received feedback that separate measurement is complex and costly, and produces information that some users do not find useful:

---

[6] Improvements to the impairment requirements in IAS 36 would also be considered under Approaches G1 and G2.

[7] The detailed staff analysis of these approaches is in March 2016 Agenda Paper 18A, February 2016 IASB Agenda Paper 18A and November 2015 Agenda Paper 18A.

(i) some customer-related intangible assets, in particular customer relationships;

(ii) brand names;

(iii) non-contractual intangible assets;

(iv) intangible assets that are not capable of being sold or licensed separately. These are also being considered by the FASB, as is restricting this to

- noncompetition agreements; and/or
- customer-related intangible assets that are not capable of being sold or licensed independently;

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

(vi) intangible assets in the early stage of development.

(b) Indefinite life intangible assets that are difficult to value on an individual basis (subsuming those assets in goodwill would not increase pressure to amortise goodwill unless those assets are subsequently reassessed as having a finite life).

(c) The types of intangible assets that would not be capitalised if they were internally generated, for example research, customer relationships, brands, etc. However, whilst this would result in accounting consistent with the accounting for internally generated intangible assets, it would result in an inconsistency with the accounting for intangible assets that are acquired separately.

Approach T3 Subsume intangible assets that cannot be measured reliably

15. Remove statement in IFRS 3/IAS 38 that an acquirer can always reliably measure the fair value of identifiable intangible assets acquired in a business combination (ie reverse change made in 2008). Some respondents think that removing this criterion in 2008 increased concerns that entities need to recognise some intangible assets, such as customer relationships and brands, that are complex and subjective to measure and for which separate recognition may not provide useful information.

Approach T4 Allow further grouping of intangible assets

16. Allow further grouping of intangible assets, ie relax the requirement for when a group of complementary intangible assets can be recognised and measured as a single asset (currently permitted only if they have similar useful lives).[8] For intangible assets that are difficult to value on an individual basis, this might permit accounting together with other intangible assets (as a 'portfolio' of intangible assets).

Approaches to address users' presentation and disclosure concerns

17. Presentation: require entities to provide further disaggregation of amortisation on the face of the statement of comprehensive income/income statement to enable users to distinguish between acquired intangible assets that would not be capitalised if internally generated (eg customer relationships) and those that would (eg software).

18. Disclosures: require entities to provide disclosures in IFRS 13 *Fair Value Measurement* about the valuation methods and assumptions used for significant intangible assets acquired in a business combination. Currently, assets and liabilities acquired in a business combination do not fall within the disclosure requirements of IFRS 13 on the date of acquisition.

Staff observations and proposed next steps

19. The staff think there needs to be a strong argument to support making further significant changes to IFRS 3 for goodwill and other intangible assets:

    (a) Stakeholders have always had opposing and strongly held views on subsequent accounting for goodwill, in particular amortisation versus non-amortisation. The feedback during the IFRS 3 PIR did not provide evidence that this diversity has decreased, of new conceptual arguments, or that goodwill amortisation provides useful information to investors. Furthermore, the data research presented by the ASBJ/EFRAG staff did not provide evidence that goodwill balances are growing excessively (see paragraph 6).

[8] Paragraph 37 of IAS 38 permits an acquirer to recognise a group of complementary intangible assets as a single asset provided the individual assets have similar useful lives.

(b) Since 2004 the Board has amended the requirements for intangible assets in a business combination twice[9], each time requiring more intangible assets to be identified separately from goodwill. Subsuming additional intangible assets in goodwill would increase the amount of goodwill. This could increase concerns about goodwill overstatement, about lack of amortisation and about lack of rigor in the impairment test for goodwill.

20. The staff propose the following steps to address the issues identified in the PIR:

(a) Step 1: Our primary focus should be improving the impairment requirements. This alone could result in sufficient improvements and could address the main concerns heard in the PIR about goodwill without the need to consider other changes to the accounting for goodwill.

(b) Step 2: Improve the guidance about intangible assets acquired in a business combination. The current guidance in the illustrative examples in IFRS 3(2008) was based on IFRS 3(2004), which itself was based on earlier US guidance. This guidance dates back more than ten years. Since the guidance was developed there have been developments in the nature and valuation of intangible assets. Consequently the staff think the first step in addressing concerns about identifying and measuring intangible assets should be to consider whether updating the guidance in IFRS 3 could help to mitigate some concerns about the complexity of applying the requirements. In Appendix A, the staff have provided some analysis on how we might approach this for customer-related intangible assets.

(c) Step 3: Improve the information provided to investors about goodwill and other significant intangible assets acquired in a business combination. Agenda Paper 18B considers possible improvements to the disclosures for goodwill. Paragraphs 17-18 of this paper suggest two approaches we may want to consider for other intangible assets.

[9] Both on issue of IFRS 3(2004) and issue of IFRS 3(2008). Paragraphs 7-9 of February 2016 Agenda Paper 18A described the changes made.

Appendix A: Feedback from the IFRS 3 PIR on subsequent accounting for goodwill

A1. The Board's report and feedback statement on the PIR of IFRS 3 provided the following possible next steps to address subsequent accounting for goodwill:

Area of focus	Assessed significance	Possible next steps
Subsequent accounting for goodwill (ie impairment-only approach compared with an amortisation and impairment approach).	High	Research will be undertaken. We could consider whether and how the costs of accounting for goodwill can be reduced without losing the information that is currently being provided by the impairment-only approach, and which our review of academic studies suggested was value-relevant. This could include considering: (a) how improvements to the impairment-only approach (in particular to the impairment test) could address some of the concerns that have been raised; and (b) whether a variation on an amortisation and impairment model could be developed with an amortisation method that does not undermine the information currently provided by the impairment-only approach.

A2. Many participants during the PIR suggested reintroducing amortisation of goodwill because they state that it reflects consumption of the economic resource acquired in the business combination over time. Some suggested this could be reintroduced with an indicator based impairment test rather than an annual test, reducing cost and complexity.

A3. Some investors supported an impairment only approach because they think that this approach helps them to assess the stewardship of management and assess whether an acquisition is working as expected. Other investors support the amortisation of goodwill, because they think that goodwill acquired in a business combination is consumed and replaced by internally-generated goodwill over time.

Appendix B: Feedback in the IFRS 3 PIR on identification and measurement of intangible assets

B1. The Board's report and feedback statement on the IFRS 3 PIR provided the following possible next steps to address identification and measurement of intangible assets:

Area of focus	Assessed significance	Possible next steps
Identification and fair value measurement of intangible assets such as customer relationships and brand names.	Medium/high	Research will be undertaken. We could consider whether particular intangible assets (eg, customer relationships) should be subsumed into goodwill. We could also consider what additional guidance could be given to assist in the identification of customer relationship intangible assets and their associated measurement.

B2. The PIR identified concerns that, for some intangible assets, measurement at fair value is costly (because of the need to use valuation specialists), complex and time-consuming. The PIR also identified that some users of financial statements say that the valuations of some intangible assets are subjective and do not provide useful information. Customer relationship intangible assets were the most frequently cited examples by preparers, users and other parties. Brands were also commonly cited. Consequently some participants in the PIR think the benefit of the information provided to users about these intangible assets does not justify the costs of separately recognising them. Nevertheless, some users support recognising these intangible assets separately because it provides an insight on why an acquisition was made and about the primary assets/value drivers of the acquiree.

B3. Some participants also stated that the following other intangible assets are challenging to measure (and also in some cases to identify):

(a) non-contractual intangible assets.

(b) intangible assets that are not capable of being sold or licensed separately.

(c) intangible assets for which there is no active market.

(d) intangible assets in the early stage of development.

B4. The main challenges identified during the PIR in measuring intangible assets were:

(a) the assumptions used in valuation models and in estimating the useful life are difficult to determine and are subjective. Valuation models are sometimes sensitive to small changes in those assumptions.

(b) there are various valuation methods and there is diversity on when/how they are used.

(c) when there are multiple intangible assets, judgement is needed not only to value them individually but also to determine relationships between them. For example customer relationships would need to be considered in determining the fair value of an acquired brand.

B5. The staff have identified the following as the two main concerns we have heard from users of financial statements during the PIR about the presentation and disclosure of intangible assets in a business combination:

(a) Presentation of amortisation expense: Some users have concerns that amortising intangible assets that they consider to be continually replaced, such as brands and customer-related intangible assets, results in double counting of expenses. For this reason they want to add back the amortisation charge on these intangible assets to derive an underlying earnings number. However, they say they are often unable to differentiate between amortisation they want to add back and amortisation they wish to keep in profit. Although this information should be available from the intangible asset reconciliation (see paragraph 118(e) of IAS 38) some users have said it should be available on the face of the statement of comprehensive income because of its importance and/or because they need the distinction to be available in interim/quarterly reports (where the note reconciliation may not be provided).

(b) Additional disclosure: Some users have told us that there is insufficient information about the assumptions used in valuations models for intangible assets acquired in a business combination and in the assessment of their useful lives. Some noted that it would be useful to require the disclosures in IFRS 13 *Fair Value Measurement* on valuation techniques and inputs for these intangible assets.

Appendix C: Draft staff analysis of guidance for customer-related intangible assets

Introduction

C1. Since the IFRS 3 illustrative examples were developed there have been developments in the nature and valuation of customer-related intangible assets. For example:

(a) Many entities are now using sophisticated databases to collect much more data about their customers, for example about their demographics, preferences, relationship history and prior buying patterns. Data can be used to improve an entity’s own profitability, for example through better knowledge of what customers want and for internet advertising, or sold on to other entities. These changes in the nature and amount of data collected, and the ways it is used, means customer data is becoming more valuable.

(b) When customer loyalty plans first appeared they primarily included relatively straight forward plans, such as frequent flyer miles, to encourage repeat transactions by customers. Today, many more entities are using customer loyalty plans, both to reward customers and as a means to collect data about them (as in (a)). These plans come in many different forms. These changes in the nature and extent of loyalty schemes are one way that customer relationships are evolving.

C2. Based on the feedback received during the PIR, customer-related intangible assets, in particular customer relationships, appear to be the most challenging intangible assets to measure separately from goodwill. Furthermore, in 2007 the IFRIC received a request to provide guidance on the circumstances in which a non-contractual customer relationship arises in a business combination. The IFRIC decided sufficient confusion and diversity in practice existed to warrant attention (see appendix D).

C3. At the March 2016 Board meeting a few Board members stated that there was a need to better define what a customer relationship is and how to distinguish it from other customer-related intangible assets.

C4. For these reasons, in this appendix the staff have considered what we might want to address in reconsidering the current guidance for customer–related intangible assets.

Requirements for customer-related intangible assets in business combination

C5. IFRS 3 requires an acquirer to recognise, separately from goodwill, all identifiable intangible assets acquired in a business combination. Paragraph 12 of IAS 38 *Intangible Assets* states that an intangible asset is identifiable if it:

(a) is separable, ie is capable of being separated or divided from the entity and sold, transferred, licensed, rented or exchanged, either individually or together with a related contract, identifiable asset or liability, regardless of whether the entity intends to do so; or

(b) arises from contractual or other legal rights, regardless of whether those rights are transferable or separable from the entity or from other rights and obligations.

C6. Paragraph IE23 in the IFRS 3 illustrative examples provides the following examples of customer-related intangible assets acquired in a business combination:

Class	**Basis**
Customer lists	Non-contractual
Order or production backlog	Contractual
Customer contracts and related customer relationships	Contractual
Non-contractual customer relationships	Non-contractual

Paragraphs IE24-IE31 of IFRS 3 provide further information about these classes.

Staff analysis

Interaction of customer-related intangible assets with other intangible assets

C7. The staff think it is important to establish the boundaries between different classes of customer-related intangible assets to avoid double counting the same economic benefits. For example, when either party to a customer contract has a right to cancel or renew that contract, there may be a grey area as to whether potential economic benefits relate to existing customer contracts or to customer relationships. In other words, it may be unclear where existing contracts end and possible future contracts start. Contract boundary questions have led to much discussion in other areas, for example in the insurance contracts project.

C8. The staff think it may also be important to clarify the boundaries between customer-related intangible assets and other intangible assets, for example brands. Based on the staff's discussions with valuers, the staff understands that at the time the guidance in IFRS 3 was written brands were generally valued using the relief from royalty method. However, these days brands in the consumer product sector are often considered the primary intangible asset acquired and are valued using excess earnings methods, and customer relationships are often incorporated in that valuation. This could result in double counting if an amount is also included as a separate customer-related intangible.

C9. The staff think a clear description of the different classes of customer-related intangible assets may help to mitigate these issues.

Reconsidering the different classes of customer-related intangible assets

C10. The staff think that revising the classes of customer-related intangible assets in paragraph IE23 of IFRS 3 as follows may be helpful and have explained their reasoning below:

Class	**Basis**
Customer data	Non-contractual
Rights and obligations under customer contracts	Contractual
Customer relationships	Non-contractual

'Customer data' and 'customer relationships' would not be contractual assets because they exclude all rights and obligations under contracts.

Note, further disaggregation of these classes may be appropriate depending on the entity's facts and circumstances.

Customer data

C11. Paragraph IE24 of IFRS 3 notes that a customer list consists of information about customers, such as their names and contact information. It also notes that a customer list may be in the form of a database that includes other information about the customers, such as their order histories and demographic information.

C12. In paragraph C1, the staff have observed that an increasing number of companies are collecting much more data about their customers, beyond basic contact information.

This means customer databases are becoming more significant assets. Consequently the staff think that the Board may wish to consider whether this class of customer-related intangible assets should be called ‘customer data’ rather than ‘customer lists’. An entity could further disaggregate this class, for example between:

(a) customer lists, which contain specific contact information for customers.

(b) customer databases, which may consist of other information collected about customers.

C13. The staff do not think the basis for recognising customer data separately from goodwill should depend on how the data arose, ie whether or not the customer has, or had, a contract with the entity. However, the staff note that the entity's right to use the data may depend, at least to some extent, on the customer's consent, for example through terms of business or agreeing to a privacy policy. Nevertheless, the staff think that if rights and obligations relating to customer contracts are considered as a separate class (discussed further below), then all other customer-related intangible assets should be non-contractual. Under the current requirements in IFRS 3 this would mean that customer data acquired in a business combination would be recognised separately from goodwill only if it is separable.

C14. In some jurisdictions specific contact information may be restricted from transfer by data protection regulations. However, general, anonymous data about buyer preferences and demographics, might be more freely transferred. If customer data is no longer considered ‘contractual’, this factor may become significant in determining whether customer data is measured separately from goodwill.

Rights and obligations under customer contracts

C15. Paragraph IE23 of IFRS 3 currently lists an ‘order or production backlog’ and ‘customer contracts and the related customer relationships’ as two examples of classes of customer-related intangible assets. Furthermore:

(a) Paragraph IE25 states that an order or production backlog arises from contracts such as purchase or sales orders.

(b) Paragraph IE27 states that a customer contract and the related customer relationship may represent two distinct intangible assets. However, whilst paragraph IE28 provides guidance on when a customer relationship exists, the guidance does not provide information on the boundaries between a customer contract and a customer relationship.

C16. The staff think it would be more appropriate to replace these two examples of classes by the following: 'rights and obligations under contracts' and 'customer relationships'. An order or production backlog that arises from contracts such as purchase or sales orders would constitute rights and obligations under a contact.

C17. The staff think that the contractual rights and obligations that exist under a contract should be considered separately from the customer relationship asset. Nevertheless, as noted in paragraph C7, there is a grey area between rights and obligations under existing contracts and customer relationships when one party or the other has a right to cancel or renew the contract (ie where do existing contracts end and where do possible future contracts start). However, the staff think that a typical market participant would take into account possible renewals or cancellations in determining the fair value of the rights and obligations under a contract.

Customer relationships

C18. In addition to rights and obligations under contracts, there is a possibility of repeat business, cross-selling etc., because the customer has established a relationship with the entity.

C19. Considering the definition of an asset in the Conceptual Framework Exposure Draft, the staff think that if a customer relationship is considered to be an asset it might best be described as:

> the present right to receive any future net economic benefits that flow from having a relationship with a customer beyond any contractual rights, and excluding right to use, licence or sell any data held about that customer and also excluding any other intangible asset.

C20. Because a customer relationship asset represents rights beyond any contractual rights, it would always be non-contractual. This may help to address some of the concerns about the distinction between contractual and non-contractual customer relationships that were considered by the IFRIC (see Appendix D). Under the current requirements in IFRS 3 this would mean that customer relationships acquired in a business combination would be recognised separately from goodwill only if separable.

C21. Paragraph IE28 currently provides the following guidance about when customer relationships exist:

> A customer relationship exists between an entity and its customer if (a) the entity has information about the customer and has regular contact with the customer and (b) the customer has the ability to make direct contact with the entity.
> Customer relationships may arise through means other than contracts, such as through regular contact by sales or service representatives.

C22. The staff think that the criteria in paragraph IE28 would provide evidence of a customer relationship, but does not think it would capture all customer relationships. For example, while the staff think there would need to have been some interaction with the customer to give rise to a relationship, the staff does not think it would be necessary for there to have been a past contract or regular contact between the customer and the entity. For example, a customer may have taken free advice from a health practitioner many years ago, but not entered into a contract with the practitioner, nor had any contact since. Nevertheless, the staff think a customer relationship may still exist in this scenario. For example if the person has a health concern in the future, the likelihood of that person returning to the same practitioner may be higher because of that past contact.

C23. The staff think it might be helpful to develop the criteria in paragraph IE28 to help entities identify its customer base with which customer relationships may exist. The staff think that if customers are not known to the entity, then any potential relationship with those potential customers should be subsumed within goodwill, or part of another intangible asset such as a brand.

Appendix D: IFRIC agenda decision in March 2009 IFRIC update newsletter

D1. The following IFRIC agenda decision[10] has been extracted from the March 2009 edition of IFRIC update.

IFRS 3 Business Combinations—Customer-related intangible assets

The IFRIC received a request to add an item to its agenda to provide guidance on the circumstances in which a non-contractual customer relationship arises in a business combination. IFRS 3 (as revised in 2008) requires an acquirer to recognise the identifiable intangible assets of the acquiree separately from goodwill. An intangible asset is identifiable if it meets either the contractual-legal criterion or the separable criterion in IAS 38. Contractual customer relationships are always recognised separately from goodwill because they meet the contractual-legal criterion. However, non-contractual customer relationships are recognised separately from goodwill only if they meet the separable criterion.

The IFRIC noted that the IFRS Glossary defines the term ‘contract’. Paragraphs B31─B40 of IFRS 3 provide application guidance on the recognition of intangible assets and the different criteria related to whether they are established on the basis of a contract. The IFRIC also noted that paragraph IE28 in the illustrative examples accompanying IFRS 3 provides indicators for identifying the existence of a customer relationship between an entity and its customer and states that a customer relationship ‘may also arise through means other than contracts, such as through regular contact by sales or service representatives.’

The IFRIC concluded that how the relationship is 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. The IFRIC noted that the criteria in paragraph IE28 might be more relevant. The existence of contractual relationships and information about a customer’s prior purchases would be important inputs in valuing a customer relationship intangible asset but should not determine whether it is recognised.

In the light of the explicit guidance in IFRS 3, the IFRIC decided that developing an Interpretation reflecting its conclusion is not possible. Noting widespread confusion in practice on this issue, the IFRIC decided that it could be best resolved by referring it to the IASB and the FASB with a recommendation to review and amend IFRS 3 by:

- removing the distinction between ‘contractual’ and ‘non-contractual’ customer-related intangible assets recognised in a business combination; and
- reviewing the indicators that identify the existence of a customer relationship in paragraph IE28 of IFRS 3 and including them in the standard.

[10] IFRIC agenda decisions are not Interpretations.