Staff paper

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Project	**Business Combinations—Disclosures, Goodwill and Impairment**
Topic	**Other IAS 36 proposals**
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Purpose and structure

1. As Agenda Paper 18 explains, this paper summarises feedback about some of the proposals to amend IAS 36 *Impairment of Assets* in the Exposure Draft *Business Combinations—Disclosures, Goodwill and Impairment* (Exposure Draft). In particular, this paper summarises:
   (a) feedback on the proposed requirement to disclose in which reportable segment a cash-generating unit (CGU) or group of CGUs containing goodwill is included;
   (b) feedback on the proposed removal of the requirement to use pre-tax cash flows and discount rate when calculating value-in-use (VIU)—that is, allowing the use of post-tax cash flows and discount rates; and
   (c) other feedback on IAS 36.

2. This paper is structured as follows:
   (a) key messages (paragraphs 3–4);
   (b) feedback summary (paragraphs 5–19); and
   (c) question for the IASB.

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Key messages

3. Most respondents agree with the proposed requirement to disclose in which reportable segment a CGU or group of CGUs containing goodwill is included and say the information would be useful and/or would not be costly to disclose. Some say this proposal would not reduce management over-optimism. A few auditors and regulators, while not necessarily disagreeing with the proposed requirement, say management over-optimism is not a problem.

4. Almost all respondents agree with removing the requirement to use pre-tax cash flows and pre-tax discount rates when calculating VIU—that is, allowing the use of post-tax cash flows and discount rates. However, many request guidance on how to incorporate tax effects when calculating VIU on a post-tax basis.

Feedback summary

5. The following paragraphs summarise feedback on:

   (a) the proposal to disclose in which reportable segments a CGU or group of CGUs containing goodwill is included (paragraphs 7–12); and

   (b) the proposal to allow use of post-tax cash flows and discount rates (paragraphs 13–17).

6. Paragraphs 18–19 summarise other feedback on IAS 36.

Disclosing in which reportable segments a CGU (or group of CGUs) containing goodwill is included

Background

7. The IASB proposed to require an entity to disclose in which reportable segment a CGU (or group of CGUs) containing goodwill is included. Paragraph BC202 of the Basis for Conclusions on the Exposure Draft (Basis for Conclusions) explains that in

the IASB's view, this information would, amongst other things, help users of financial statements (users) better assess the reasonableness of assumptions used in the impairment test and thereby reduce management over-optimism.

Feedback

8. Most respondents agree with the proposal for reasons consistent with those considered by the IASB. Some disagree—paragraphs 9–10 summarise their reasons. A few provide suggestions of other ways to reduce management over-optimism—paragraphs 11–12 summarise those suggestions.

Reasons for disagreeing

9. Some respondents disagree with the proposal. A few of them disagree that management over-optimism is a problem and/or that overly optimistic estimates of cash flows is best addressed by auditors and regulators.[1] These respondents say, for example:

   (a) management and those charged with governance—and not external parties such as auditors and regulators—have primary responsibility for the reasonableness of assumptions and estimates;

   (b) robust standard-setting—not enforcement mechanisms—should address these matters;

   (c) established management processes and regular auditor challenges already address potential over-optimism; and

   (d) IAS 36 sufficiently safeguards against management over-optimism by requiring entities to disclose key assumption and sensitivity analysis.

[1] Paragraph BC189 of the Basis for Conclusions states 'In developing its preliminary views in the Discussion Paper, the IASB observed that:…(c) overly optimistic estimates of cash flows are best addressed by auditors and regulators, instead of by changing IFRS Accounting Standards.'

10. A few other respondents say the disclosure might not be as useful as the IASB intends because, for example:

    (a) it will be difficult for a user to reconcile CGU-level assumptions and segment-level information when a reportable segment contains multiple CGUs. The proposed disclosure could confuse, rather than help, users in such situations.

    (b) the disclosure will only be provided by entities applying IFRS 8 and not all entities applying IFRS Accounting Standards.

Suggestions

11. A few respondents suggest introducing other disclosure requirements, either instead of, or in addition to the proposal. These include requiring an entity to disclose:

    (a) a comparison of previous cash flow forecasts with actual results. This could help assess the accuracy of management's historical estimates.

    (b) a comparison of key assumptions with, and explanation of significant differences from, market parameters.

12. A few respondents say the IASB could better achieve its aim of avoiding management over-optimism by providing guidance on how to calculate terminal value.

Allowing use of post-tax cash flows and discount rates

Background

13. As paragraph BC215 of the [Basis for Conclusions] explains, in calculating VIU, IAS 36 requires an entity to use pre-tax cash flows and discount them using pre-tax discount rates. To reduce the cost and complexity of the impairment test, the IASB proposed to remove this requirement. Consequently, an entity would be able to use either pre-tax or post-tax cash flows and discount rates to calculate VIU. The IASB also proposed to require an entity to disclose whether the discount rate used is pre-tax or post-tax.

14. Paragraphs BC215–BC222 of the Basis for Conclusions explain the IASB's rationale for the proposal.

Feedback

15. Almost all respondents agree with the proposal for reasons consistent with those considered by the IASB (see paragraph BC219 of the Basis for Conclusions).

16. A few respondents disagree and say the proposal could lead to diversity in practice unless the IASB provides additional guidance (explained in paragraph 17).

17. In developing the proposals, the IASB considered requests from stakeholders to provide further guidance and illustrative examples to help entities calculate VIU using post-tax cash flows and discount rates. Paragraph BC220 of the Basis for Conclusions explains why the IASB decided not to do so. Many respondents request further guidance and illustrative examples. Respondents request:

    (a) additional guidance for, and/or disclosures of, tax effects such as:

        (i) clarifying how to reflect deferred taxes included in the carrying amounts of CGUs in cash flow projections;

        (ii) how to treat tax losses and other tax credits; and

        (iii) disclosure of the approach used for reflecting tax effects and an explanation of key assumptions related to tax consequences;

    (b) clarifying whether the choice between calculating VIU on a pre-tax or a post-tax basis is an accounting policy choice requiring consistent application;

    (c) guidance on how to transition from using pre-tax cash flows and pre-tax discount rates to using post-tax cash flows and post-tax discount rates; and

    (d) guidance on the use of post-tax cash flows and discount rates for specific industries or situations—for example, for financial institutions; or for foreign currency cash flows.

Suggestions for other changes to IAS 36

18. Some respondents provide feedback on the IASB’s approach to make targeted amendments to the impairment test to reduce management over-optimism and shielding. One preparer explicitly welcomes the IASB's decision not to make fundamental changes to the impairment test and instead to provide helpful clarifications. However, other respondents say a more fundamental change to IAS 36 is required to address the concern about impairment losses sometimes being recognised too late. In addition to suggesting the re-introduction of goodwill amortisation (see Agenda Paper 18A of the IASB’s December 2024 meeting):
    (a) one respondent regrets the IASB did not pursue the headroom approach it considered earlier in the project[2]; and
    (b) one respondent says the impairment model relies too heavily on estimates.

19. Respondents suggest other amendments to IAS 36 beyond those proposed, for example:
    (a) one suggests revising example 9 of the Illustrative Examples accompanying IAS 36 (which illustrates disclosure for CGUs containing goodwill) to illustrate the proposed disclosure requirements; and
    (b) one suggests strengthening the requirements to use reasonable and supportable assumptions through additional application guidance.

Question for the IASB
Do IASB members have any questions or comments on the feedback in this agenda paper?

[2] See paragraphs BC190–BC191 of the Basis for Conclusions for an explanation of the headroom approach and feedback on that approach.