Accounting Standard

AASB 1013
June 1996

Accounting for Goodwill

Issued by the
Australian Accounting Standards Board

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Defined words appear in *italics* the first time they appear in a section. The definitions are in Section 13. Standards are printed in **bold** type and commentary in light type.

MAIN FEATURES OF THE STANDARD

The Standard prescribes the accounting treatment for goodwill and discount on acquisition arising on acquisition of a business entity, or part thereof, through acquisition of the assets, or in the case of an investment in a subsidiary or in an associated company, through the acquisition of some or all of the shares in another entity. The Standard also prescribes the accounting treatment for internally generated goodwill.

The main revision to the superseded Accounting Standard AASB 1013 "Accounting for Goodwill" is that the straight-line method of amortisation has been prescribed.

The Standard has been presented in plain English format, consistent with the approach adopted in recent standards and exposure drafts issued by the Board. However, aside from amendments to effect the revision outlined above, the requirements of the Standard remain the same as those of the superseded Standard.

ACCOUNTING STANDARD

AASB 1013 "ACCOUNTING FOR GOODWILL"

1 Application

1.1 Subject to paragraph 1.2, this Standard applies to each *entity* which is required to prepare *financial statements* in accordance with Part 3.6 of the Corporations Law and which:

(a) is a *reporting entity*; or

(b) holds those financial statements out to be, or form part of, a *general purpose financial report*.

1.2 Where a requirement of this Standard is inconsistent with any provision of the Corporations Law or the Corporations Regulations, the requirement does not apply.

1.2.1 The standards specified in this Standard apply to the *financial report* where information resulting from their application is material, in accordance with Accounting Standard AASB 1031 "Materiality".

2 Operative Date

2.1 This Standard applies to *financial years* ending on or after 30 June 1996.

2.2 This Standard may be applied to financial years ending before 30 June 1996 where an election has been made in accordance with subsection 285(3) of the Corporations Law.

2.3 When operative, this Standard supersedes Accounting Standard AASB 1013 "Accounting for Goodwill" as approved by notice published in Gazette No. S 110 on 18 April 1988 and amended by Accounting Standard AASB 1025 "Application of the Reporting Entity Concept and Other Amendments".

2.3.1 Notice of this Standard was published in the *Commonwealth of Australia Gazette* on 14 June 1996.

3 Purpose of Standard

3.1 The purpose of this Standard is to:

(a) specify the manner of accounting for *goodwill* and *discount on acquisition* on the acquisition of an *entity*, or part thereof; and

(b) require disclosure of information relating to goodwill so that users of *financial reports* are provided with information about the financial position and performance of the entity.

4 Internally Generated Goodwill

4.1 *Goodwill* which is internally generated by the *entity* must not be *recognised* by that entity.

4.1.1 Goodwill which is internally generated by an entity is not permitted by this Standard to be recognised as an asset by that entity. This is principally because of the difficulty, or impossibility, of identifying the events or transactions which contribute to the overall goodwill of the entity. Even if these were identifiable, the extent to which they generate future benefits and the value of such benefits are not usually capable of being measured reliably. Internally generated goodwill which is not recognised as an asset will either go completely unrecognised or will be recognised as an expense.

5 Purchased Goodwill

Accounting Treatment for Purchased Goodwill

5.1 *Goodwill* which is purchased by the *entity* must be *recognised* as a non-current asset at acquisition.

5.1.1 Consistent with the definition of assets as service potential or future economic benefits controlled by the entity as a result of past transactions or other past events, this Standard specifies that goodwill is an asset. In particular, goodwill comprises the future benefits from *unidentifiable assets* which, because of their nature, are not normally individually recognised. Examples of unidentifiable assets include market penetration, effective advertising, good labour relations and a superior operating team. Unidentifiable assets do not include assets of an intangible nature which are capable of being both individually identified and separately recognised, as may be the case with patents, licences, rights and copyrights.

5.1.2 A distinction is frequently drawn between goodwill which is purchased and goodwill which is internally generated. This Standard specifies that the concept of goodwill as an asset is the same regardless of whether it has been purchased in an exchange transaction or generated internally. However, purchased goodwill can be measured more reliably, on the basis of the amount paid for it, than can internally generated goodwill which is not usually capable of being measured reliably. Consequently, the accounting treatment for purchased goodwill differs from that specified for internally generated goodwill.

5.1.3 Goodwill is recognised as an asset only when it satisfies the following asset recognition criteria:

(a) it is probable that the future benefits embodied in the unidentifiable assets will eventuate; and

(b) it possesses a cost or other value that can be measured reliably.

5.1.4 This will be the case only when goodwill is purchased in connection with the acquisition of an entity, or part thereof, through acquisition of the assets therein or, in the case of an investment in a *subsidiary*, the acquisition of some or all of the shares in another entity. Such purchased goodwill reflects: future benefits which are internally generated by the vendor prior to the date of acquisition and are expected to flow to the purchaser; and future benefits which arise from the combination or inter-relationship of entities or groups of assets.

5.2 Purchased goodwill must be amortised so that it is recognised as an expense in the profit and loss account on a straight-line basis, over the period from the date of acquisition to the end of the period of time during which the benefits are expected to arise.

This period must not exceed twenty years from the date of acquisition.

5.2.1 In accordance with paragraph 5.4, the unamortised balance of goodwill must be reviewed as at each *reporting date* and recognised in the profit and loss account as an expense to the extent that future benefits are no longer probable.

5.2.2 In order to amortise goodwill over the period during which the associated benefits are expected to arise, separate assessments may need to be made in respect of different goodwill components (such as those relating to the purchase of different businesses) to the extent that such components can be separately identified.

5.2.3 Factors which are to be considered in estimating the useful lives of the assets comprising goodwill include:

(a) effects of obsolescence, demand and other economic factors; and

(b) the service life expectancies of individual employees or groups of employees; and

(c) expected actions by competitors or potential competitors; and

(d) relevant legal, regulatory or contractual provisions; and

(e) foreseeable life of the entity or industry.

5.2.4 Because the period of anticipated benefits will in many circumstances be difficult to identify, decisions concerning the period of amortisation may be arbitrary. In some circumstances the period of amortisation may be short, but in no circumstance does this Standard permit the amortisation period to exceed twenty years from the date of acquisition.

5.3 Subject to paragraph 5.2, the period over which goodwill is to be amortised must be reviewed as at each reporting date and, if necessary, adjusted to reflect the amount and timing of expected future benefits. The period must not extend beyond twenty years from the date of acquisition.

5.4 The unamortised balance of goodwill must be reviewed at each reporting date and recognised as an expense in the profit and loss account to the extent that future benefits are no longer probable.

5.5 Other than required by paragraph 5.4, purchased goodwill must not be revalued.

Measurement of Purchased Goodwill

5.6 On acquisition of an entity, or part thereof, through acquisition of the assets therein or, in the case of an investment in a subsidiary, on acquisition of some or all of the shares ofanother entity, the identifiable net assets of the entity (acquired directly or indirectly) must be measured at their *fair values*.

5.6.1 In determining the amount of purchased goodwill the purchaser needs to recognise all assets acquired, whether of a tangible or intangible nature. This might involve recognising some intangible assets which, if internally generated by the purchaser, would not normally be recognised as assets because the absence of an exchange transaction usually prevents them from being measured reliably.

5.6.2 Fair value is a measure of the worth of an asset at a specified time, and is utilised in this Standard as the amount which the purchaser attributes at the date of acquisition to the *identifiable assets* acquired. When making an assessment of the fair values to be attributed to individual assets, the purchaser may sometimes find that a number of such assets are combined into a related or composite group. In these circumstances, it may be more appropriate to consider the fair value of the composite group rather than the aggregate of the fair values of the individual assets.

5.7 Goodwill which is purchased by the entity must be measured as the excess of the *cost of acquisition* incurred by the entity over the fair value of the identifiable net assets acquired.

5.7.1 The *purchase consideration* may include any one, or combination, of the following:

(a) cash; and/or

(b) other monetary assets; and/or

(c) non-monetary assets; and/or

(d) securities issued; and/or

(e) liabilities undertaken.

5.7.2 Where the purchase consideration includes cash and/or other monetary assets, its value is usually readily determinable. However, where the purchase consideration comprises (either partially or totally) non-monetary assets, its value will need to be ascertained by reference to the fair values of the non-monetary assets given.

5.7.3 Where the purchase consideration comprises shares or other securities of the purchaser and these securities are listed publicly on an Australian Stock Exchange, the price at which they could be placed in the market will usually be an indication of their fair value. Where the securities issued are those of an unlisted entity, it may be necessary to make a valuation of those securities. It should not be assumed that the par value of securities reflects their fair value, as this rarely is the case.

5.7.4 Where an entity incurs costs that directly relate to the acquisition, these need to be included in the determination of the cost of acquisition. These costs would normally include legal fees, stamp duty and other government charges, and professional fees in the nature of feasibility tests and investigations preceding acquisition.

5.8 To the extent that the cost of acquisition incurred by the entity exceeds the fair value of the identifiable net assets acquired but the difference does not constitute goodwill, such difference must be recognised immediately as an expense in the profit and loss account.

6 Subsequent Changes in Cost of Acquisition

6.1 Where it is probable that the *cost of acquisition* will vary, because it is contingent upon one or more future events, and the amount of the variation can be estimated reliably at the date of acquisition, such an amount must be included in the calculation of the cost of acquisition. Where the amount of the variation

cannot be reliably estimated at the date of acquisition, an accrual for the amount must be *recognised* as soon as it can be estimated reliably.

6.1.1 The cost of acquisition may vary, contingent on one or more future events. When a variation is probable and the amount of the variation can be estimated reliably at the date of acquisition, it needs to be included in the calculation of the cost of acquisition. If any additional payment cannot be estimated reliably at the date of acquisition, an accrual for the additional payment needs to be made as soon as the amount can be estimated reliably.

6.2 Where a variation in the cost of acquisition depends upon a contingency which affects the determination of the *fair value* of net assets of the acquired *entity*, an adjustment to the individual assets or liabilities and to the *purchase consideration* must be made. Where the contingency does not affect the value of the net assets of the acquired entity, the acquiring entity must treat the variation as an adjustment to the purchase consideration, thereby increasing or decreasing the amount of *goodwill* or *discount on acquisition*.

6.2.1 The accounting treatment of any variation of the cost of acquisition depends upon the nature of the contingency. Where the contingency affects the determination of the fair value of net assets (such as the valuation of receivables or inventory, or the identification of liabilities) of the acquired entity, an adjustment to the individual assets or liabilities and to the cost of acquisition needs to be made. On the other hand, where the contingency does not affect the value of the net assets of the acquired entity, for example, where it relates to the level of earnings of the acquired entity, the acquiring entity treats the variation as an adjustment to the cost of acquisition. The adjustment in this instance has the effect of either increasing or decreasing the amount of goodwill or discount on acquisition.

7 Subsequent Identification of Assets and Liabilities

7.1 Where it becomes known, subsequent to acquisition, that assets or liabilities existed at the date of acquisition but were not

recognised**, an adjustment must be made in respect of those assets and liabilities and, where relevant, in respect of the**

amount of *goodwill* or *discount on acquisition*. A similar adjustment must also be made where assets and liabilities which were unidentifiable at acquisition subsequently become identifiable.

8 Discount on Acquisition

8.1 Where the *fair values* of the identifiable net assets acquired by the *entity* exceed the *cost of acquisition* incurred by the entity, the difference represents a *discount on acquisition* and must be accounted for by reducing proportionately the fair values of the non-monetary assets acquired until the discount is eliminated. Where, after reducing to zero the recorded amounts of the non-monetary assets acquired, a discount balance remains it must be *recognised* as a revenue in the profit and loss account.

8.1.1 Where the fair values assigned to the identifiable net assets acquired exceed the cost of acquisition, this Standard specifies that the difference represents a discount on acquisition. This discount may reflect a bargain purchase and/or compensation in anticipation of temporary future losses or inadequate future profits. The discount on acquisition is to be accounted for by reducing proportionately the fair values of the non-monetary assets acquired until the discount is eliminated. In the rare circumstance that, after reducing to zero the recorded amounts of the non-monetary assets acquired, some of the discount remains, this discount balance must be recognised as a revenue in the profit and loss account.

8.1.2 This accounting treatment is consistent with the cost method because the assets acquired are recognised at their discounted amounts which aggregate to the cost of the acquisition.

9 Treatment of Goodwill or Discount on Acquisition of a Subsidiary

9.1 On acquisition of a *subsidiary*, the accounting treatment for *goodwill* which is purchased by the *entity* (including any amortisation thereof) and *discount on acquisition* must be effected as an adjustment in the *consolidated accounts* and not in the subsidiary's or *parent entity*'s *accounts*.

10 Disclosures

10.1 In respect of the amount of *goodwill recognised*, the following must be disclosed:

(a) the unamortised balance of goodwill at the *reporting date*; and

(b) the amount of goodwill amortised as an expense in the *profit and loss account* for the *financial year*, including any amount recognised as an expense in the profit and loss account in accordance with paragraph 5.4; and

(c) the period over which goodwill is being amortised.

10.2 Any amount recognised as an expense in the profit and loss account in accordance with paragraph 5.8 must be disclosed together with details of its nature and the reason for this accounting treatment.

11 Comparative Information

11.1 Subject to 11.2, the *financial report* must disclose information for the preceding corresponding *financial year* which corresponds to the disclosures specified for the current financial year.

11.2 If the disclosure requirements in paragraphs 10.1 and 10.2 have not previously applied to the *entity*, the information required by paragraph 11.1 need not be disclosed.

12 Transitional Provisions

Application of the Straight-Line Method

12.1 Whether or not the superseded Standard applied to the *entity*, where the straight-line method of amortisation of *goodwill* is not already being applied as at the beginning of the *financial year* to which this Standard is first applied, the straight-line method must be applied prospectively to the unamortised balance of goodwill as from the beginning of that financial year.

12.1.1 Where an entity was applying a method of amortisation not permitted by this Standard to allocate the cost of purchased goodwill, paragraph 12.1 prescribes prospective application of the straight-line method to the unamortised balance. The period over which the unamortised balance is amortised must not exceed twenty years from the date of acquisition. Prospective application of the straight-line method of amortisation would result in the unamortised balance of purchased goodwill being amortised in equal amounts over the remaining useful life, unless an additional write-down is required in accordance with paragraph 5.4.

Superseded Standard Applied to Entity

12.2 If the superseded Standard applied to the entity, an amount of goodwill arising in relation to the acquisition of an entity, or part thereof, included in the *financial statements* as at the beginning of the financial year to which the superseded Standard was first applied is deemed to have been determined in accordance with this Standard.

12.2.1 Any credit balance arising in relation to the acquisition of an entity, or part thereof, included in the financial statements as at the beginning of the financial year to which the superseded Standard was first applied must already have been adjusted against the carrying amounts of non-monetary assets acquired or against retained profits or accumulated losses, in accordance with the superseded Standard.

Superseded Standard Did Not Apply to Entity

12.3 If the superseded Standard did not apply to the entity, where there is included in the financial statements as at the beginning of the financial year to which this Standard is first applied an amount of goodwill or a credit balance arising in relation to the acquisition of an entity, or part thereof, that amount must be deemed to have been determined in accordance with this Standard. Where the amount is a credit balance, it must be accounted for by reducing proportionately the carrying amounts of those non-monetary assets acquired which continue to be held. Where a credit balance remains after the carrying amounts of such non-monetary assets have been reduced to zero, the remaining balance must be adjusted against retained profits or accumulated losses as at the beginning of the financial year to which this Standard is first applied.

12.3.1 The transitional provision set out in paragraph 12.3 acknowledges that there will be companies which have either goodwill or *discount on acquisition* balances existing at the beginning of the financial year to which this Standard is first applied and that such balances need to be accounted for subsequently in the financial years to which this Standard applies. The accounting treatment applied to such existing balances is to be consistent with the broad principles required by this Standard.

13 Definitions

13.1 In this Standard:

***accounts* is defined in the Corporations Law**

***consolidated accounts* is defined in the Corporations Law**

***cost of acquisition* means the *purchase consideration* plus any costs incidental to the acquisition**

date of acquisition* means the date on which the risks and rights to future benefits, as would be conferred with ownership, pass to the acquiring *entity

discount on acquisition* means the saving or allowance in the *cost of acquisition* that flows to the purchaser on acquiring shares or other identifiable net assets at less than their *fair value

***economic entity* means a group of entities comprising the *parent entity* and each of its subsidiaries**

***entity* means any legal, administrative, or fiduciary arrangement, organisational structure or other party (including a person) having the capacity to deploy scarce resources in order to achieve objectives**

***fair value* means the amount for which an asset could be exchanged between a knowledgeable, willing buyer and a knowledgeable, willing seller in an arm's length transaction**

***financial report* means *accounts* or *consolidated accounts* or both**

***financial statements* is defined in the Corporations Law**

***financial year* is defined in the Corporations Law**

***general purpose financial report* means a *financial report* intended to meet the information needs common to users who are unable to command the preparation of reports tailored so as to satisfy, specifically, all of their information needs**

goodwill* means the future benefits from *unidentifiable assets

identifiable assets* means those assets which are capable of being both individually identified and specifically *recognised

***identifiable net assets* means *identifiable assets* less liabilities**

***parent entity* means an entity which controls another entity**

***profit and loss account* is defined in the Corporations Law**

***purchase consideration* means the fair value of assets given or share capital issued, liabilities undertaken, and other securities given by the purchaser, in exchange for assets (net, where applicable) or shares of another entity**

***recognised* means reported on, or incorporated in amounts reported on, the face of the profit and loss account or balance sheet (whether or not further disclosure of the item is made in the notes thereto)**

***reporting date* means the end of the *financial year* to which the accounts or consolidated accounts relate**

***reporting entity* means an entity (including an *economic entity*) in respect of which it is reasonable to expect the existence of users dependent on *general purpose financial reports* for information which will be useful to them for making and evaluating decisions about the allocation of scarce resources, and includes but is not limited to the following:**

(a) a listed corporation;

(b) a borrowing corporation; and

(c) a company which is not a *subsidiary* of a holding company incorporated in Australia and which is a subsidiary of a foreign company where that foreign company has its securities listed for quotation on a stock market or those securities are traded on a stock market

***subsidiary* means an entity which is controlled by a parent entity**

***unidentifiable assets* means those assets which are not capable of being both individually identified and specifically recognised.**

CONFORMITY WITH INTERNATIONAL AND NEW ZEALAND ACCOUNTING STANDARDS

Conformity with International Accounting Standards

As at the date of issue of this Standard, compliance with this Standard will ensure conformity with International Accounting Standard IAS 22 "Accounting for Business Combinations", issued by the International Accounting Standards Committee to the extent that IAS 22 addresses accounting for goodwill except for the following:

(a) Where an entity applies a period of amortisation exceeding five years, it would be required to disclose a justification of the period adopted in order to comply with IAS 22.

(b) This Standard requires that a discount on acquisition be eliminated proportionately against the fair values of non-monetary assets and where the values of such non-monetary assets are reduced to zero, any remaining discount must be recognised as revenue. Under IAS 22, any remaining discount should be treated as deferred income and amortised to the profit and loss account over a period not exceeding five years unless a longer period, not exceeding twenty years from the date of acquisition, can be justified.

(c) Under this Standard, assets and liabilities acquired as part of a business acquisition which are identified and recognised subsequent to acquisition are accounted for by adjusting goodwill or discount on acquisition. Under IAS 22, any adjustments made after the end of the first financial year subsequent to acquisition are recognised as revenue or expense rather than as adjustments to goodwill or discount on acquisition.

(d) In addition to the disclosure requirements of this Standard, IA S 22 requires a reconciliation of movements in balances of goodwill, discount on acquisition and related amortisation during the financial year.

Conformity with New Zealand Accounting Standards

As at the date of issue of this Standard, compliance with this Standard will ensure conformity with Statement of Standard Accounting Practice SSAP 8 "Accounting for Business Combinations" issued by the New Zealand Society of Accountants to the extent that SSAP 8 addresses accounting for goodwill.