" A proposed model for the goodwill impairment test"

"An Applied study"

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Abstract

The goodwill is one of the most controversial topics. Especially after the financial standards transition from the amortization to the goodwill impairment approach. The goodwill impairment test faced more problems of cost, complicated and time consuming that led the financial statements preparers to disregard the goodwill impairment losses in the financial statement. Furthermore, there are more of CEOs and Financial managers manipulate with the goodwill impairment losses for their managerial discretions. All these mentioned problems led FASB, Topic350 to simplify the test by removing the second step of the goodwill impairment test that responsible for determining the goodwill impairment losses by comparing between the implied fair value of goodwill and the carrying amount of

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goodwill. But this simplification opened a large space for manipulating and personal judgment when implementing the test and determining the goodwill impairment losses. So the researcher proposed an indicator for solving these problems by using the applying study. This study focused on testing the relationship between the recorded goodwill and the revenue that arises from the sale of goods or rendering of services and predicting the future goodwill. After that comparing the current goodwill and the future goodwill to determine if there are goodwill impairment losses or not. This study concluded that this indicator has the capability of determining and predicting the goodwill impairment losses without manipulation or personal judgment because this indicator is easy to use. It doesn't cost and it saves time.

Keywords:The goodwill, The goodwill impairment test, The goodwill impairment losses,FASB,SFAS141&142, FASB,Topic350, IAS36, IFRS3.

الملخص

تعد الشهرة واحدة من الموضوعات المثيرة للجدل. خاصة بعد تحول معايير المحاسبة المالية من منهج الاستهلاك إلى منهج انخفاض الشهرة.حيث واجه اختبار انخفاض الشهرة الكثير من المشاكل من حيث إنه معقد ومكلف ويتطلب الكثير من الوقت مما جعل معدى القوائم المالية يتجاهلوا تنفيذ هذا الاختبار. بالإضافة إلى كثير من رؤساء مجلس الإدارات والمديرين الماليين قد يتلاعبوا بخسائر انخفاض الشهرة من أجل اتجاهاتهم الإدارية .كل هذه المشاكل دفعت مجلس معايير المحاسبة الأمريكي إلى تبسيط اختبار انخفاض الشهرة من خلال حذف الخطوة الثانية من الاختبار وهى الخطوة المسئولة عن تحديد خسائر انخفاض الشهرة وذلك بمقارنة القيمة العادلة الضمنية للشهرة بقيمتها الدفترية.ولكن حذف الخطوة الثانية من الاختبار فتح مجالاً كبيراً للتلاعب والحكم الشخصى عند اجراء اختبار اتخفاض الشهرة وتحديد خسائرها.

لذلك قامت الباحثة بإجراء دراسة تطبيقية لتطبيق النموذج المقترح حيث ركزت هذه الدراسة على اختبار العلاقة بين الشهرة المسجلة والايراد الناتج عن بيع سلعة أو تأدية خدمة، والتنبؤ بالشهرة المستقبلية من خلال المقارنة بين الشهرة الحالية والمستقبلية لتحديد ما إذا كان هناك خسائر انخفاض أم لا. وخلصت هذه الدراسة إلى أن هذا المؤشر لديه القدرة على تحديد خسائر انخفاض الشهرة و التنبؤ بها بدون تلاعب أو حكم شخصي. لان هذا المؤشر سهل الاستخدام وليس مكلف ولا يتطلب الكثير من الوقت.

الكلمات الافتتاحية:- الشهرة ،اختبار انخفاض الشهرة ،خسائر انخفاض الشهرة، ,FASB,SFAS141&142, FASB,Topic350, IAS36, IFRS3.

Introduction

There are increasing for the importance of the goodwill as an intangible asset, especially after the transition from the pooling of interest method to the purchasing method, when the phenomena of business combinations appeared, from this point the goodwill has been recorded on the balance sheet. But it was written down, after that the goodwill has been subjected for amortization, but the amortization approach has been accused that it doesn't reflect the economic reality of the goodwill.

So in 2001 FASB transition to the goodwill impairment approach. The goodwill impairment approach has the capability of reflecting the economic reality and the financial position with accuracy more than the amortization approach. FASB stated that the goodwill must be subjected to the goodwill impairment test mandatory annually or more if there are events or circumstances. The test has been implemented under FASB, by comparing between the carrying amount of goodwill and its fair value, but IASB by comparing between the carrying amount of goodwill and the recoverable amount. From here, the goodwill impairment test faced

problems of cost, complicated and time- consuming.

Research Problem

The problem of this research is that implementing the goodwill impairment test annually or more is very complicated, costly and it takes more time that made the test benefits is less than the incurred cost. So more of the financial statements preparers evade of implementing the test and manipulate of the goodwill impairment losses by disregarding it in the financial statement.(FASB,Topic360,2014,p1). All the mentioned problems led the financial managers and CEOs to evade of recognizing of the goodwill impairment losses. For protecting their managerial discretions and financial positions. All these mentioned problems are shortcomings of the goodwill impairment approach. Especially, the test is based on measuring with the fair value that leads to many manipulations and personal judgment. Thus, all these deficiencies provide the users with financial information isn't accurate. So there is a need for a new solution for solving all these mentioned problems.

Importance of Research

This research introduces a solution for the goodwill impairment test problems of cost, complicated and time consuming by suggesting the revenue that arises from the sale of goods or renders of services as a proposed indicator for predicting the goodwill impairment losses without estimates and personal judgment. Thus, closing all the manipulation, thus providing the users with financial information is accurate.

Research Objective

This research aims to propose a new model for testing the goodwill for impairment that is based on using the revenue as an indicator of the goodwill impairment.

Research Hypotheses

This research tests the hypothesis as follows:-

- There is a positive relationship between the recorded goodwill and the revenue that arises from the sale of goods or renders of services.

Research Methodology

For achieving the research objective and test the research hypothesis, the researcher used an applied study.

- An applied Study.

This study aims to test the relationship between the recorded goodwill and the revenue that arises from the sale of goods or renders of services and predict of the future goodwill, after that comparing between the future goodwill and the current goodwill to determine if there is a goodwill impairment loss or not. This study based on two statements that are the balance sheet and income statement by the financial statements that listed on the Egyptian Stock Exchange and the companies' sites that have goodwill.

Research Limitations

This research interested in the purchased goodwill. So this research focuses on the consolidated financial statements of companies that subjected to merger or acquisition, thus have goodwill in the financial statements. The researcher collected these financial statements from

companies listed on the Egyptian Stock Exchange and the companies' sites. This research excludes the companies that don't record goodwill in the financial statements.

Research organization:

Introduction:

Chapter one: "The goodwill impairment approach under FASB&IASB"

Chapter two: "The proposed model for the goodwill impairment test".

Chapter three: Conclusions, Results, and Recommendations.

"The conceptual framework of goodwill"

Goodwill is one of the most controversial intangible assets. This controversy arises from the nature of goodwill which is almost impossible to quantify. So more of the standards setters and researchers interested in it. Conceptually, the goodwill is future economic benefits arising from the other assets acquired in a business combination that are not individually identified and separately recognized. (Kieso et al. ,2012, p674). According to SFAS142, Goodwill is the excess of the cost of an acquired entity over the net of the amounts assigned to assets acquired and liabilities assumed. (FASB, SFAS142, 2001, p80).

Goodwill arising

The goodwill arises as a result of increasing the competition in the market, the desire of companies to achieve the greatest profit and provide the customer with the best services and products. The goodwill has two types, internally generated goodwill and purchased goodwill. Internally generated goodwill is that has been built up over time and

cannot be verified objectively.(Triest,2008, p149).It cannot be capitalized on the balance sheet, but it's recorded as an expense in the income statement.(Kieso et al.,2012,p674).The purchased goodwill arises as a result of business combinations. It is defined as the difference between the amount paid and the net assets of (tangible and intangible) and liabilities. (Kieso et al.,2012,p674)

The accounting treatment of goodwill

Anciently, many standards treated the goodwill with writing off against equity reserves accounts in the year of acquisition. (Seetharaman,2004, p140). It is written down only when the carrying amount of goodwill exceeds its implied fair value. (Jerman and Manzin, 2008,p220). After that APB Opinion No.17 stated that goodwill should be amortized over a period that cannot exceed 40 years. (Jerman and Manzin,2008,p224).

But more problems faced the amortization approach of goodwill. The most problems faced the purchased goodwill are that there is difficulty in determining the useful life for the amortization of goodwill and the arbitrary ceiling because the traditional amortization method by using the straight line of goodwill over an arbitrary period doesn't reflect the economic reality and doesn't provide with useful information to the users of the financial statements. (Qasim, 2013, p65).

So in2001, FASB transition from the amortization to the goodwill impairment approach. When the fair value of goodwill exceeds its carrying amount ,the impairment happens.(FASB,SFAS142 ,2007,P12). The test must be implemented annually or more if there are events or circumstances occur.

There are two steps for performing the goodwill impairment test. (IAS36, 2010,P3).

The First Step: Compare the carrying amount of the unit, including the goodwill, with its recoverable amount.

The second step: Compare the implied value of goodwill with its carrying amount. Any excess of the carrying amount of goodwill over its implied value is recognized immediately, in profits and losses, as an impairment loss. Any remaining excess of the carrying amount of the unit over its recoverable amount is recognized as an impairment loss and allocated to the other assets of the unit on a prorated basis, based on the carrying amount of each asset in the unit.

"Goodwill impairment test under FASB & IASB"

There is a difference between FASB&IASB with regard to the first step of the goodwill impairment test. Under FASB the test has been implemented by comparing between the carrying amount of the goodwill and its fair value.(FASB, SFAS142,2001,P15).But under IASB, the test has been implemented by comparing between the carrying amount and recoverable amount. (IAS36, 2010, P3).

Although the transition from the amortization to the impairment approach, the goodwill impairment test faced more problems of cost, complicated and time-consuming. These problems led the financial managers and CEOs to manipulate in implementing the test by disregarding the goodwill impairment losses in the financial reports for their managerial discretions. (Stephen, 2016, p16). So FASB & IASB

hold joint project concluded that FASB, Topic350 canceled the second step of the goodwill impairment test for simplifying the test. (FASB, Topic350, 2017, p2). But this simplification opens to more manipulation and personal judgment. Thus the financial information under the goodwill impairment test isn't accurate. So there is a need for a better solution for solving these problems and closing all the manipulation and personal judgment.

"Applying a proposed model for the goodwill impairment test"

According to the mentioned problems, the researcher suggested a new indicator to determine if there is a goodwill impairment or not at the same time avoid all the mentioned problems before. The standard setters indicated that there is a possibility to use a qualitative indicator for determining if there is an impairment or not, but until now the standard setters don't indicate for a specific solution or indicator. So the researcher tried to find a solution to these problems. So the researcher proposes a new model for implementing the goodwill impairment test by using an applied study to test the relationship between the revenue and the recorded goodwill. This proposed indicator has been applied to actual companies.

"The Applied Study"

1.Introduction:

Because of the problems of the goodwill impairment test, the researcher interested to introduce a solution to these difficulties. So the researcher suggested the revenue as an indicator for predicting the

goodwill impairment losses by testing the relationship between the recorded goodwill and the revenue. This research only applies to the companies that have been subjected to merger or acquisition, thus it has been recorded goodwill in the financial statement.

2. Study aim.

This study aims to test the relationship between the recorded goodwill and the revenue, predict of the future recorded goodwill, Also predict of the goodwill impairment losses by comparing between the future goodwill and the current goodwill to determine if there is a goodwill impairment loss or not. The researcher applied this indicator for confirming that this indicator has the capability of predicting the goodwill impairment losses without the mentioned problems. The researcher thinks that this indicator is easy to apply, it doesn't take more time, and it doesn't cost. This indicator will be tested in the Egyptian environment.

3. Study Hypotheses

For testing the relationship between the revenue and the goodwill, the researcher used these hypotheses:-

H0: There isn't a significant positive relationship between the recorded goodwill and the revenue.

H1: There is a positive significant relationship between the recorded goodwill and the revenue.

4.Study methodology

This study is based on the regression analysis to measure the relationship between the revenue and the recorded goodwill. This study

collects the data from the financial statements of some companies. The research measured the relationship between two variables to illustrate the ratio that the revenue able to explain the change that happens in the recorded goodwill.

5.Study community

This study just applied to the companies that have been subjected for merger or acquisition process, thus it has a recorded goodwill in the financial statement.

6.Study Sample:

The researcher used actual financial statements of the companies that have the following conditions:-

- The financial statements of the companies that have been subjected to merger or acquisition process thus have goodwill.
- The companies that published their financial statements from 2009 to 2016. The researcher chose this period after the financial crisis that happened in 2008 when many researchers accused the fair value that it is the first responsible for the financial crisis. Thus, it's not suitable for implementing the goodwill impairment test.
- These companies that have been subjected to the goodwill impairment test under FASB& IASB and disclosed in the financial statements.

Although the research community is 107 approximately, the researcher applied to five companies that are a part of the original community. These companies are McDonald's, Samsung, Orascom for Construction

and Industry, Nestle and Coca-Cola). The researcher excluded the companies that didn't comply with FASB&IASB, the companies that didn't publish the financial statements from 2009 to 2016.For explaining and analyzing the relationship between the recorded goodwill and the revenue. The researcher used the following equation:-

$$y = a + Bx + error.$$

Y ⟶ is the predicted value for the dependent variable;⟶ Y is the recorded or purchased goodwill.

X ⟶ is the Independent variable that explains the change of the dependent variable; X ⟶ is the Revenue.

A ⟶ Constant, Interpret the value of Y when X = 0

B ⟶ it measures the slope of regression line; it is the rate of change in Y with a unit change in X.

E ⟶ it is a random error.

This analysis is implemented on the revenue and the goodwill of the following companies:-

1-McDonald's company.

Mcdonald's

In Million USD	2009	2010	2011	2012	2013	2014	2015	2016
Total Revenue	22,745	24,075	27,006	27,567	28,106	27,441	25,413	24,622
Rcorded goodwill	2,425	2,586	2,653	2,804	2,873	2,735	2,516	2,337

2-Samsung company.

Samsung

In million USD	2009	2010	2011	2012	2013	2014	2015	2016
Total of Revenue	136,323.67	154,630.33	165,001.77	201,103.61	228,692.67	206,205.99	200,653,482	201,866,745
Recorded goodwill	9.885	83.462	523.409	573.845	560.534	739.576	910,539	1,343,580

3- Orascom for construction and industry company.

Orascom For Construction and Industry								
In Million USD	2009	2010	2011	2012	2013	2014	2015	2016
Total of revenue	21312.8	27552.4	32722	33287	6212.9	7846.5	3882.4	4033.1
Recorded goodwill	9871.2	10599.9	11055.6	9059.3	6099.3	6276.5	13.8	13.8

4- Nestle company.

Nestle								
In millions USD	2009	2010	2011	2012	2013	2014	2015	2016
Revenue of sales	99,361	104,972	83 642	92,186	92,158	91,612	88,785	89,469
Recorded goodwill	27,502	27,031	29,008	32,615	31,039	34,557	32,772	33,007

5- Coca cola company.

Coca Cola								
In Million USD	2009	2010	2011	2012	2013	2014	2015	2016
Revenue	30,990	35,119	46,542	48,017	46,854	45,998	44,294	41,863
Recorded goodwill	4,224	11,665	12,219	12,255	12,312	12,100	11,289	10,629

The statistical results by SPSS

Correlation Table (1/1)

		Recorded goodwill	Revenue
Recorded goodwill	Pearson correlation		.851**
Revenue	Pearson correlation	.851**	

**Correlation is significant at the 0.01 level (2-tailed).

Regression Table (1/2)

R	R Square	Adjusted R Square	Std.Error of the Estimate	B	
				Constant	Revenue
0.851	0.724	0.716	158440.742	5606.896	0.003

Results analysis:-

Regarding, the correlation analysis, there is a positive relationship between the recorded goodwill and the revenue with (.85+). Also, p-Value is equal to 0.000 that is less than the significance level, 5%, so we reject the null hypothesis that indicated there isn't a positive relationship between the recorded goodwill and the revenue. And we accept the alternative hypothesis that indicated there is a positive relationship between the recorded goodwill and the revenue.

Regarding, the regression analysis, we find that the independent variable explains 72% of the changes that happened in the dependent variable. So we find that the revenue explains 72% of the changes that happened in the goodwill. Thus, the researcher suggests that using the revenue as an indicator for predicting of the goodwill impairment. And the remaining 28% is due to some other variables that are included in the regression equation that is y = 5606.896 +0.03x.

Explaining the results and comments:-

Table (1/3)

Table of variance and regression analysis

Source	DF	SS	MS	F	P-Value
Regression	1	2,497E+12	2,497E+12	**99.479**	**0.000[b]**
Error	38	9,539E+11	25103468831	-	-
Total	39	3,451E+12	-	-	-

It is clear from the table of variance analysis that P-Value is equal to Zero that is less than significant level 5%. Thus we accept the main

hypothesis, that indicates that there is a significant relationship with statistical significance between the recorded goodwill and the revenue. And reject that the null hypothesis that indicates for there isn't a significant relationship with statistical significance between the recorded goodwill and the revenue.

Implementation of the proposed indicator.

The researcher implemented the revenue as a proposed indicator for applying to Coca-Cola company to illustrate how to predict the goodwill impairment. The researcher used 2016 as an application year.

Coca Cola							
In Million USD	2009	2010	2011	2012	2013	2014	2015
Revenue	30,990	35,119	46,542	48,017	46,854	45,998	44,294
Recorded goodwill	4,224	11,665	12,219	12,255	12,312	12100	11,289

The statistical results by SPSS

Correlation Table (1/4)

		Recorded Goodwill	Revenue
Recorded Goodwill	Pearson Correlation		.803**
Revenue	Pearson Correlation	.803**	

**Correlation is significant at the 0.01 level (2-tailed).

Regression Table (1/5)

R	R Square	Adjusted R Square	Std.Error of the Estimate	B	
				Constant	Revenue
0.803	0.644	0.573	1929.208	-4216.237	0.355

The analysis' results

Regarding the correlation analysis, there is a positive relationship between the recorded goodwill and the revenue with (.803+).

Regarding, the regression analysis, we find that the independent variable explains 80.3% of the changes that happened in the dependent variable. So we find that the revenue explains 80.3%of the changes that happened in the goodwill. Thus, the researcher suggests that using the revenue as an indicator for predicting of goodwill impairment. And the rest 19.7% indicates for other factors include the random error.

From the following figure, we can write the equation as follows:-

y=a+bx ⟶ y= .355X-4216.237.

In case we have the revenue of 2016 as follows (41,863). We can apply the equation and predict the recorded goodwill in 2016. The following result shows that the predictive value of the recorded goodwill 2016 is 10645 $ instead of 10629 $. When comparing the goodwill recorded in 2015 and 2016. We find that there is a decline of 644 million dollars at the goodwill that is the goodwill impairment losses. So this proposed indicator has the capability to solve the problems of the goodwill impairment test.

Summary of the analytical and comparative study

This study confirmed that the proposed indicator has the capability of predicting the goodwill impairment losses easily without the mentioned problems before and without estimation or personal judgment.

Conclusion

This research concluded that the goodwill is one of the most controversial and difficult intangible assets. After, the transition from the amortization to the impairment approach, the goodwill becomes so complex. There are more difficulties when implementing the goodwill impairment test of costly, complex and time-consuming. All these mentioned problems led more financial statements preparers to disregard implementing the test because the test benefits less than the incurred costs. Additionally, more of CEOs disregard the goodwill impairment losses in the financial reports for their managerial discretions .

Although FASB, Topic350 canceled the second step of the goodwill impairment test to simplify. The test still has difficulties and subject to personal judgment. So the researcher suggested an indicator for predicting the goodwill impairment losses without manipulation by the applied study that concluded that this indicator has the capability of predicting the goodwill impairment without more cost, complicated, and time-consuming, because this indicator is easy to use, doesn't cost and saves time.

Results:

This study concluded that the proposed indicator able to predict of the recorded goodwill easily without all the problems of the goodwill

impairment test of cost, complex and time-consuming. Furthermore, it is capable of closing all the manipulations by using the revenue that arises from the sale of goods or renders of services. This indicator can determine the recorded goodwill for next year because there is a positive relationship between the goodwill and the revenue. After that, the researcher can determine the losses by comparing the currently recorded goodwill and the last year to determine if there is an impairment loss or not.

Recommendations.

For decreasing the difficulties of the goodwill impairment approach,

1. The researcher recommends developing the current goodwill impairment test.
2. The researcher recommends closing all the manipulations and estimations by using the regression analysis to determine the extent of the capability of the proposed indicator to explain the recorded goodwill for predicting with the next recorded goodwill.

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Entrepreneurial orientation, networks and performance: an empirical study of SMEs in Egypt

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Abstract

Building on the resource orchestration literature, we use a two step technique through structural equation modelling to test a model where entrepreneurial orientation (EO)mobilizes resources to influence SMEs performance. Using survey data from 180 SMEs in technical industry sectors, our results indicate that EO mediates (partially) social capital - firm performance relationships. This finding drive managers to understand that networks provide critical base for entrepreneurial activities, however, building large, high quality networks is essential to mobilize resources within EO to develop competitive advantage and achieve superior and positive firm performance.

Introduction

Entrepreneurial orientation (EO) is reflected in its three core dimensions: innovativeness, risk-taking and proactiveness; and has a positive effect on firm performance (Hean, Thi, & Ping, 2007; Rauch, Wiklund, Lumpkin, & Frese, 2009; William J Wales, Patel, Vinit, & Kreiser, 2013). Previous studies highlight that firms with high EO are more able to capture opportunities, adjust its operations in the marketplace to enhance performance and increase profitability (Y.-H. Li, Huang, & Tsai, 2009; Stam & Elfring, 2008). EO improves firm performance by facilitating firm's ability to identify innovative opportunities with greater