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AMBIGUITY OF GOODWILL REGULATIONS – A CASE OF POLISH PUBLICLY TRADED ENTERPRISES

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***Abstract**: Because goodwill appears as a consequence of consolidation process as well as business combinations, it is a regular item in statements of financial position prepared by modern entities. Polish publicly traded companies are obliged to follow international or Polish accounting standards that both include regulations referring to goodwill. Although Polish standard-setters are aiming at accounting harmonization, Polish legislature is not fully converged with international standards. Moreover, international standards are not precise enough to oblige accounting professionals to act in a certain way when measuring goodwill. Freedom of action arising from ambiguity of choices should be used in a way to achieve relevance and faithful representation of financial information. Through the analysis of European Union and Polish accounting regulations authors suggest that legal foundations of goodwill disclosure and measurement should be more detailed. A survey conducted among Polish publicly traded companies acknowledges that goodwill is a complicated item in financial reports and that is why accounting professionals should pay more attention to disclosed information in order to achieve fundamental qualitative characteristics. Authors' contribution into the modern accounting literature is twofold. First, authors call for a greater attention to significance of information about goodwill, especially on economic substance of goodwill disclosed in financial reports, verifiability, understandability, and a risk regarding changes in estimates included in goodwill valuation process. Second, the importance of right teaching methods is pointed out in order to stress that arithmetical calculations following legal regulations of goodwill are not satisfactory for faithful representation of economic substance of goodwill.*

***Keywords**: goodwill, business combinations' accounting, IFRS 3, Polish accounting*

INTRODUCTION

The ongoing combinations of business entities have resulted in gathering economic resources and it enabled many economies to develop and create big industrial organizations. Large-scale entities are important performers on the contemporary capital markets and because of that they are subject of significant importance to the financial well-being of the economy and the nation. It is useful, therefore, to give some consideration to the present business combinations' accounting since financial reporting misstatement might damage the credibility of accounting that is essential to the effectiveness of contemporary capital markets.

The combination of business enterprises comes as a result of the acquisition by one entity (acquirer, acquiring company) of the assets of another entity (acquiree, acquired company) on an ongoing concern basis, either directly (as a merger or acquisition) or indirectly (acquisition of the voting control of the shares of the acquired company). Business combination may be followed by a legal merger (non-consolidation merger; hereafter: non-consolidation goodwill) or may be established by a parent company when buying shares in another entity (consolidation; hereafter: consolidation goodwill). Consolidation goodwill appears in the group financial reports only (consolidated reports) while non-consolidation goodwill may be disclosed in either an individual company financial report or in a consolidated financial report.

The initial valuation of goodwill arising from business combination and the subsequent disposition of goodwill once recorded have gained a lot of research efforts of the accounting profession in the recent years. Its main focus was concentrated on the fundamental difference between pooling and purchase methods of accounting for business combinations and clear statement that the choice of accounting method should not be within management's option. Before the 1950s, the purchase method was prevailing but in the 1960s the predominance of pooling of interests method was observed. The application of purchase method diminished due to 'the goodwill issue', which arose as a result of unchanged book values of net assets acquired and their comparison to the market value of the purchase price. On that account the large amount of goodwill was booked on the day of acquisition that diminished equity on the same day or in the following years. While purchase method required write-off of goodwill decreasing retained earnings (or other positions of equity), the pooling approach accepted summarizing the incomes of combining entities resulting in increased profitability of the entity operating after the merger. Different approaches to goodwill and a need to escape from the constraints of purchase method resulted in the wide acceptance of the pooling approach. Popularity of pooling of interests method also forced accounting theoreticians and standard-setters to crystallise its principles and to clearly indicate the border between the application of pooling of interests method and the purchase method. The controversy relating to business combinations is still a continuing debate although pooling of interests method was restricted in the U.S. in 2001 and in the content of International Financial Reporting Standard in 2004. Weaknesses of contemporary regulations pointed out in the present literature are concentrated on the goodwill accounting, both initial valuation and its subsequent disposition or lack of subsequent disposition.

The article deals with the issue of information disclosure of goodwill arising from consolidation (consolidation goodwill) or from an acquisition (non-consolidation goodwill). The objective of financial reports is to provide summarised information that is useful to users of a financial statement in making decisions about providing resources to entity. In order to fulfil the conceptual requirements, the information provided to the users should contribute to the faithful representation of relevant information about the resources of the entity and how efficiently and effectively the entity's management has discharged its responsibilities to use entity's resources. Through the analysis of European Union and Polish accounting regulations the authors suggest legal foundations of goodwill disclosure and measurement should be more detailed. A survey conducted among Polish publicly traded companies acknowledges that goodwill is a complicated item in financial reports and that is why accounting professionals should pay more attention to information disclosed in order to achieve fundamental qualitative characteristics. Authors' contribution into the modern accounting literature is twofold. First, authors call for a greater attention to significance of information about goodwill, especially on economic substance of goodwill disclosed in financial reports, verifiability, understandability, and a risk regarding changes in estimates included in goodwill valuation process. Second, the importance of right teaching methods is pointed out in order to stress that arithmetical calculations following legal regulations of goodwill are not satisfactory for true and fair view of economic substance of goodwill.

ECONOMIC SUBSTANCE OF GOODWILL

According to contemporary accounting regulations, when the purchase price exceeds the value of net assets acquired, the difference is presented among assets in the statement of financial position. Because of the above algorithm, goodwill represents a residual after allocation of consideration paid to tangible assets, identifiable intangible assets, and liabilities.

The economic notion standing behind the goodwill position shall answer the question why has the premium, which results in goodwill, been paid for the acquired company? The premium was paid usually because the goodwill is already present and was present before business combination and expected earnings justify the consideration. Backman states (1970) that expected (in the future) earnings reflect expenditures made by acquiree in the past for management, research and development, public relations, advertising, patents, and development of staff. As a result of past expenditure it is expected to gain economic benefits in the future due to a premium management, experienced staff or established brand name (Myers, 1977, Kamela-Sowińska, 1996). Moreover, part of goodwill may represent price inflation and part may be permanent reflecting long-time customers and lists of regular customers. Furthermore, previous studies have shown that investors attach different valuation weights to various goodwill components of accounting goodwill numbers (Hirschey, Richardson, 2002). The most valuable goodwill is the one resulting from synergy effect and from going-concern of the acquired entity. The less prized by investors is residual goodwill defined as the excess of purchased goodwill over going-concern goodwill plus synergy goodwill. According to International Financial Reporting Standard No. 3 'Business combinations' goodwill represents future economic benefits arising from other assets acquired in a business combination that are not individually identified and separately recognized.

It is important to stress, that goodwill is bought, not created at the time of a business combination. Although goodwill is in existence, it is not disclosed in the statement of financial position of the acquiree before the acquisition. That means that in the absence of a business combination, the goodwill will not be recorded in the books. The inconsistency in the treatment of goodwill for acquired entities and for those not acquired arises from the confidence that internally generated goodwill shall not be disclosed in financial statement. It cannot be classified as an asset as no reliable measurement is possible in the lack of a purchase price. Because of the above assumption, the literature presents opinions that presenting goodwill for acquired company but not for the acquiring company is illogical (Kripke, 1968). On the other hand, the history of accounting shows that internally generated goodwill, which was not created in the business combination transaction, was presented in the balance sheet in the past. Nobes and Norton (1989) demonstrate that in the UK and the Netherlands, where companies write off consolidation goodwill against retained earnings, internally generated brand names were used to fulfil the 'hole in the balance sheet'.

Furthermore, goodwill does not incorporate new intangibles that are created after the combination. While on the other hand, the newly created (internally generated) goodwill may serve as an offset to the write-offs of goodwill in the years following the business combination. Goodwill shall not include overpayment for the acquired entity that arose i.e. due to mistaken fair value measurement. Previous research provides evidence that goodwill is not typically overvalued when initially recorded (Churyk, 2005), but in the situation when acquirer overpays for the acquiree the goodwill impairment should be recorded at the day of acquisition.

The magnitude of goodwill value is determined by the type of consideration and is significantly influenced by the market value of this payment. As stock prices fluctuate widely, mostly because of the factors not related to business combination, it seems obvious that the measurement of goodwill is a subject to significant distortions in a short period of time and disclosed values obsolete as the time passes. Moreover, the goodwill definition present in the accounting theory is an operational definition that simply refers to a method of measurement in order to find arithmetic difference. Neither does it point out the economic nature of goodwill nor the resources encompassed in it. Because of the above, goodwill disclosed in the financial report that is based on the measurement technicalities serves as a substitute for an asset recognition. However, in the contemporary accounting practice the residual goodwill misses more fundamental approach describing the economic substance of this position of the financial report. The issue is even more important as the opinion stating that purchased goodwill is not an asset can be found in the literature (Tollington, 1998).

TYPES OF GOODWILL

Goodwill may occur as an asset of an entity, regardless of the possibility of its verification. The occurrence of goodwill may indicate higher fair value, usually market value, of a given entity in relation to the sum of the fair value disclosed in the financial reports of net assets. From the point of view of the market functioning, the main form of verification of the occurrence or not of the goodwill as an asset of the entity is a carried out particular transaction to acquire all or part of the entity. From this point of view there can be distinguished:

- internally generated goodwill,
- purchased goodwill.

The internally generated goodwill occurs in case of a higher fair value of the entity in relation to its carrying amount. In this case, the carrying amount is understood as the value of entity's equity. The internally generated goodwill of the company may not be recognized in the financial statements as an asset of the entity and its existence may affect the conditions of a possible purchase of this entity, its organized part, or interest in it. It should be emphasized that the company's internally generated goodwill is often used for the valuation. One of the concepts of using the financial statements for purposes of determining the value of the business entity for the owners is the Hoogendoorn model (Hoogendoorn, 2000). Hoogendoorn has proposed transforming the traditional financial reports to the prospective financial reports using the internally generated goodwill of the company (Kumor, Strojek-Filus, 2013).

Purchased goodwill may be the result of the acquisition of another entity (or its organized part) then there is the following relationship between the accepted (negotiated) price and goodwill (Strojek-Filus, 2013):

Purchase price = fair value of acquired net assets + purchased goodwill

Goodwill disclosed in a particular transaction is acquired by the acquiring entity. A business entity may acquire goodwill through the purchase of the entire entity, its organised part or acquisition of shares offering control, joint control in it or allowing for exerting a significant impact on this entity. From this point of view there can be identified:

- non-consolidation goodwill purchased when buying assets in a company,
- wholly or partially purchased goodwill in a transaction done by a holding company (consolidation goodwill).

Given the nature of the financial statements in which the purchased goodwill is presented, the following can be distinguished:

— goodwill representing assets of business entity, presented in the financial statement.

— goodwill as the consolidation difference, presented as an asset of the group in the consolidated financial statement.

Goodwill as the consolidation difference is the result of implemented consolidation procedures in the entities' financial statements included in the group. One of the stages of consolidation is to establish and carry out the so-called initial consolidation of capital. As part of this step, the overvaluation of the acquired shares representing control manifested by a price surplus paid for them in relation to the fair value of net assets is determined.

From the point of presenting company's goodwill in the financial report, the following can be distinguished:

— goodwill constituting business entity's separate item of assets,

— goodwill 'hidden' under a different report item.

The latter is the case in the framework of a simplified version of the equity method, in which the purchased goodwill is recognized by the established value of the investment. Goodwill determined under the procedures of the equity method is part of the investment value in the statement of financial position[3]. The user of the financial reports is not able to assess the effect of the acquisition of shares by the analysis of goodwill or negative goodwill, as these items are not separated. They are an invisible element of the share value to the user. In this case, goodwill 'is hidden' in the carrying amount of the shares in a subordinated entity, as illustrated in Figure 1.

CARRING AMOUNT OF SHARES	
The fair value of the net assets of the subsidiary attributable to the investor according to their percentage in the share capital of the entity	Remaining goodwill

Figure 1: Structure of investments valued using the equity method

Source: own elaboration.

Goodwill, being part of the investment, is not distinguished but is a subject to accounting according to the rules laid down for the acquired or consolidated goodwill. From the standpoint of the economic effect and sense of acquiring another entity or shares in it, there can be pointed out:

— positive goodwill, called most frequently goodwill and

[3] The Accounting Act permits the use of the equity method in the separate financial reports, and in accordance with IAS/IFRS application of this method is allowed only in the consolidated financial reports.

— negative goodwill, which, depending on the solutions adopted in the accounting regulations, can be shown as a separate report item of liabilities or recognised as income in the period in which the acquisition was carried out[4].

The article deals with non-consolidation and consolidation goodwill purchased by a holding company when buying shares of another entity or acquired in the acquisition transaction resulting in legal merger of joining entities.

GOODWILL METHODOLOGY AND PRESENTATION

The excess of purchase price over the book value of the acquired company's net assets was the first accounting measurement of goodwill (positive goodwill) (Nobes, Norton, 1996). As the amount recorded as goodwill required a comparison of the fair value of consideration transferred and the book value of assets purchased, the literature presents problems in measuring the proper amount of goodwill as well as the potential occurrence of unrecorded goodwill due to the misstatement of market price. Sharp price fluctuations that accompany merger announcements and propriety of using a market price to value large blocks of stock given as a part of consideration were mentioned among other practical issues (Copeland, Wojdak, 1969).

Contemporary the calculation of goodwill requires the comparison of fair value of consideration paid with the fair value of net assets purchased. The high quality of goodwill valuation is then a consequence of properness of fair value measurement that can be complex. Moreover, estimating fair value of the consideration given may be problematic when purchase price encompasses various components in addition to the cash.

The excess of fair value over book value resulting from an acquisition was treated differently in the following years after business combination. Figure 2 exhibits the number of alternatives for subsequent disposal of goodwill that was described in the literature.

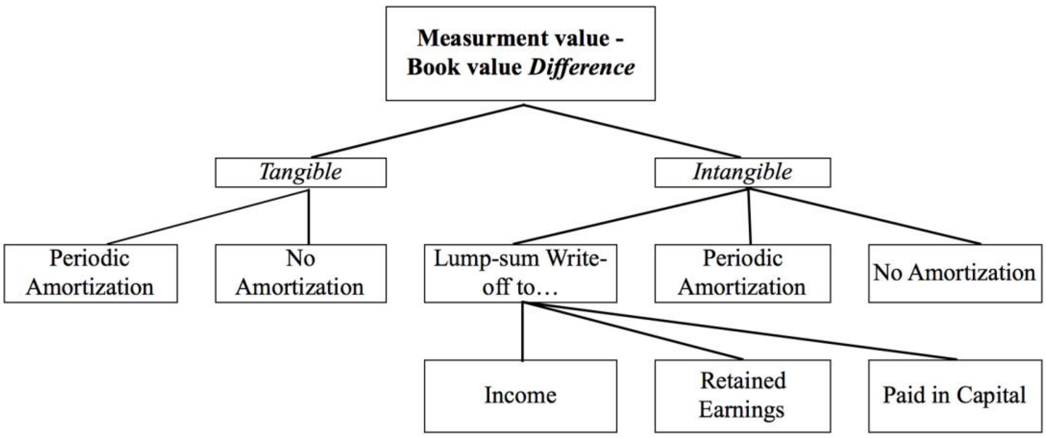

Figure 2: Accounting treatment of goodwill.

Source: Based on the goodwill classification presented by Copeland, Wojdak, 1969, p. 59.

Accounting theory accepted allocation of goodwill to tangible or intangible assets, as well partial allocation to both assets' categories. Goodwill allocated to assets was then amortized

[4] The Polish accounting regulations contain a solution that is a combination of both interpretation variants of negative goodwill.

periodically or not amortized at all. Accounting history has noticed a period when goodwill was subject to amortization only in years when earnings were unusually good. Conversely, no amortization was recorded during difficult years (Knortz, 1970). Until the mid of 1940s prevailing accounting practices of goodwill treatment included the lump-sum write-off to income, retained earnings or paid capital. Direct write-offs of goodwill to earned surplus or capital surplus have not been permitted in the USA since 1953 (Copeland, Wojdak, 1969).

The next acceptable practice was that of systematic amortization of goodwill against earnings over the period of 40 years. There was no justification of the 40-year limit other than an unofficial statement that, through the use of such an extended period, charges against earnings would be minimized. In that period of goodwill accounting history, the restatement of acquiree net assets' values was introduced. Goodwill was calculated as the positive difference between the fair (market) value of consideration paid and the fair value of net assets acquired in a business combination. In these years, the literature presents controversies referring to the deterioration in residual goodwill values. The opinion that changes in stock prices' market values should be the indicators for changes in goodwill estimates can be observed (Knortz, 1970). Knortz states that stock prices are appropriate basis for indicating whether goodwill values had been absorbed in the process of generating future economic benefits. He states that turning pages of the calendar are not sufficient evidence of diminishing value of goodwill, as these values might not necessarily be lost with the passage of time. Moreover, if an entity regularly spends money on research and development, advertising, and personnel training etc., the goodwill values are given expression in exchange price at the time of an acquisition. If these expenditures together with amortization of goodwill are charged to earnings, the revenues of a single year will bear a duplicated cost and economic profits will be understated. Backman indicates (1970) that the more is paid for the acquiree (and the larger goodwill as a consequence of a high purchase price) the less would be earned in the following years (due to goodwill amortization). In his opinion, amortization of artificially created goodwill made no economic sense and acted as an incentive to pay less for the acquired company because of the adverse effect on earnings. The adverse effect on future earnings may influence profit centres of the combined company and alter the ability to retain or employ new staff members.

Mandatory amortization of goodwill against reported earnings ended at the same time when pooling of interests method was abandoned, i.e. in 2001 in the U.S and in 2004 when IFRS 3 was published. Regulators did away with the presumption that acquired goodwill and other acquired intangible assets have finite lives and eliminated amortization. Instead of amortization, standards mandated for annual test for goodwill impairment. Goodwill shall be tested in a three-step process according to subsequent accounting for goodwill. The first phase measures the carrying amount of cash-generating unit (units) that goodwill is being allocated to at the day of the acquisition. As goodwill does not generate cash flow independently of other assets or a group of assets, it is required to allocate goodwill to an individual cash-generating unit (or units) that serves as the lowest level within the entity at which the goodwill is monitored. In the second step, the entity measures the recoverable amount of the cash-generating unit, and the third phase requires comparison of the amounts calculated in the first and second steps. If the carrying amount of the unit exceeds the recoverable amount of the unit, the entity shall recognize the impairment loss. After goodwill impairment losses are recognized, subsequent reversals of impairment are prohibited. Information about the carrying amount of goodwill must be disclosed on an annual basis, along with the estimates used in the valuation process. Goodwill write-offs are material charges against earnings that do not typically coincide with changes in tangible, other intangible assets or cash flows. Furthermore, as fair values are not readily available for many cash-generating units and require independent valuations, managers enjoy a substantial amount of discretion. The information value of write-offs disclosure lies in the role they play as a signal of changes in the future earnings potential of the entity or important implication for the ongoing value of the company (Hirschey, Richardson, 2002).

Polish accounting regulations also present the algorithm for goodwill calculations ignoring the economic sense of this financial statement position. Goodwill should be carried at cost less any accumulated amortization and any accumulated impairment losses. Therefore goodwill is not a subject to impairment but to amortization and write-offs recognition. According to Polish Accounting Act, goodwill should be amortized on a systematic basis over 5 years. There is a possibility to extend amortization period to 20 years but a non-rebuttable presumption exists that the useful life of goodwill will not exceed 20 years from initial recognition. The amortization of each period is presented as an expense in the income statement. An entity presenting goodwill from business combination should, at least at each financial year-end, estimate impairment losses of goodwill. Estimation of impairment requires valuation of recoverable amount of goodwill that is amortized. Because Polish regulations do not give any detailed guidance as to check whether impairment occurs, Polish entities should follow International Accounting Standard No 16.

Polish legislature still accepts recognition of negative goodwill. Any excess of fair value of net assets over consideration transferred is presented among liabilities as a negative goodwill. Present regulations limit the value of negative goodwill to the amount of fair value of fixed assets (excluding non-current marketable financial assets) requesting the excess to be presented as revenue at the date of business combination. The treatment of negative goodwill in the following years depends whether expected future losses and expenses occur or not. In short, present Polish legislature in the scope of negative goodwill is in accordance to International Accounting Standard inapplicable since 2004.

TECHNICALITIES OF CONSOLIDATION GOODWILL

Consolidation goodwill is also calculated as the difference between the purchase price and the fair value of what is purchased. Unlike the non-consolidation goodwill, the consolidation goodwill is the result of carrying out procedures for the consolidation of the financial statements included in the holding company. It is set within the so-called initial consolidation of equity that is the date of acquisition of shares representing the parent company’s control over a subsidiary. In terms of disclosure in the consolidated financial reports and amount of goodwill, the accepted concept of consolidation, which is the basis for solutions to the accounting law, is essential.

The literature indicates the following concepts for the consolidation of financial statements:

- proprietary concept (used in the proportional consolidation method)5,
- parent entity concept,
- parent entity extension concept, and
- business entity concept (Ignatowski, 2003).

In case of the parent entity extension concept, goodwill attributable to a majority stake is only recognized, while the part relating to the minority shareholdings is ignored. In contrast to the

[5] The proportional method is not used under the existing IAS/IFRS (IAS/IFRS – International Accounting Standards / International Financial Reporting Standards). It was replaced by the equity method, but it is allowed in the Accounting Act for the settlement of joint control relations.

methods of the parent and minority shareholdings, they are also valued at fair value. Solutions that are valid in the current wording of the basic act governing the preparation of financial reports in Poland – the Accounting Act – are in line with the parent entity extension concept.

All of the goodwill is recognized within the business entity concept in the consolidated financial reports, and therefore this part that is attributable to minority shareholdings, called for this reason non-controlling interests. Non-controlling interests in this case are stated at the fair value including goodwill related to them. The business entity concept is the basis of the solutions adopted in IAS/IFRS in the preparation of the consolidated financial reports. The valuation of non-controlling interests adopted by the parent entity is also important in this case:

- proportional valuation,
- fair value valuation.

According to the proportional method, the valuation of non-controlling interests is carried out based on the fair value of net assets acquired in the proportion attributable to the shares. In turn, the market value should be adopted as the basis for determining the fair value, if there is an active market or by reference to the value of controlling interests, taking into account discounts or other valuation methods. Using these two methods one can get different results concerning goodwill from consolidation.

The differences between the solutions in determining the goodwill of consolidation adopted in the Accounting Act and IAS/IFRS are not merely technical. These are important differences on the conceptual ground, so a different approach to demonstrate the effects of the consolidation of financial statements. The Accounting Act expressly refers to the concept of parent entity, whereas IAS/IFRS to the concept of business entity. The most serious consequences of these differences precisely focus on the level and method of goodwill presentation.

It should also be noted that the Accounting Act allows showing up to a certain amount of negative goodwill, while IAS/IFRS do not allow such a possibility, considering the negative difference in total as revenue for the period – income on the occasional purchase. The rules for determining the difference of consolidation in accordance with Art. 60 of the Accounting Act can be illustrated by the following equation:
The purchase price of the shares by the parent company (PP) – the sum of the fair value of net assets attributable to the acquired shares (NAF) = positive consolidation difference = goodwill (G)

Whereat $PP > NAF$

Goodwill is recognized as a main separate item (it cannot be combined with other items) of the consolidated statement of financial position. In the second case the purchase price is less than the sum of the fair value of the net assets of the subsidiary acquired by the proportion of shares. The above can be illustrated by the following equation:

The acquisition price of the shares by the parent company – the sum of the fair value of net assets attributable to the acquired shares = negative consolidation difference = negative goodwill (NG)

Whereas $PP < NAF$

Thus, the relevant part of the excess of net assets at fair value over the value of the shares is negative goodwill, which - in accordance with the Accounting Act - must be shown as a separate liabilities item in the consolidated statement of financial position[6].

In accordance with IFRS 3, goodwill is calculated according to an algorithm shown in Figure 3 (Strojek-Filus, 2012).

Transferred consideration (C)
+
The value of non-controlling interests in the acquiree (I)
+
The value of the share capital of the acquiree, held by the acquirer, if the merger is implemented in stages (SC)
-
The net value of identified assets acquired and assumed liabilities (AA)
=
Goodwill (G) or gain from bargain purchase (P)

Figure 3: Determination of goodwill or a gain from the bargain purchase

Goodwill occurs if C + I + SC > AA

Accounting treatment for consolidation goodwill is the same as that for non-consolidating goodwill both in international standards and in Polish accounting regulations.

It is worth noting that such a significant difference between the solutions of the Accounting Act and IAS/IFRS make the comparability of data and proper assessment of the impact of the acquisition of other entity or shares in it difficult (and sometimes impossible) in business practice. From the point of view of Polish economic practice the problem is even greater, as part of the Polish companies prepares their financial reports in accordance with IAS/ IFRS[7], and part with the Accounting Act. So the comparability is difficult also between Polish entities.

Presented accounting regulations for consolidated and non-consolidated goodwill initial valuation and measurement in subsequent years show that faithful presentation of a business combination (including goodwill arising from this transaction) requires detailed disclosure in order to enable users of financial statements to understand the economic phenomena hidden behind the accounting numbers. Disclosure should encompass inter alia methods of fair value

[6] The solutions of the Accounting Act constitute a specific hybrid variant to demonstrate the whole negative difference as negative goodwill and recognize it as revenue for the period. To the amount of the fair value of acquired assets, excluding long-term financial assets listed on regulated markets – must be shown as negative goodwill. Above this value – must be shown as income of the period and hence by a solution referring to IAS/IFRS.

[7] These are companies quoted in public trading on the basis of Regulation (EC) No. 1606/2002 of the European Parliament and of the Council of 19 July 2002 on the application of international accounting standards – International Accounting Standards. Official Journal of EC L 243, 11.09.2002.

measurement of purchase price as well of net assets acquired, financial parameters engaged in the methods, the valuation techniques used for non-controlling interests measurements, assessment of changes in goodwill valuation including cash generating units' expected cash-flows. Lack of detailed information or imprecise data in financial reports may be misleading and may cause incorrect judgment about economic situation of the entity. Significant discrepancies between Polish accounting regulations and IAS/IFRS should also be noted as they hinder the comparability of financial reports.
From the point of view of the educational process of accounting it is worth highlighting that the correct determination and interpretation by the student of goodwill requires:

- knowledge of methods and specific rules for determining the fair value of assets and liabilities,
- fluent knowledge of the scope and structure of financial statements,
- the ability to use an algorithm for determining goodwill under the current law,
- the ability to associate the causes and consequences of the financial and legal capital ties between business entities.

The indicated conditions, however, are not sufficient in the light of further amendments to IAS/IFRS and solutions laid in the Accounting Act. At present, it should also be emphasized:

- the importance of ethical attitude of accountants and managers,
- the knowledge of economic sense of goodwill and on this basis its presentation in the financial statements
- the ability to associate dispersed information in the financial statements related directly or indirectly to the formation and accounting of goodwill.

According to the authors, the teaching process in terms of goodwill requires, *inter alia*, the analysis of various cases described in the literature, but also case studies of economic practice in which they are discussed and debated taking into account different aspects of this asset.

RELATED RESEARCH AND ANALYSIS OF CASE STUDIES

On the basis of economic and accounting theory it is difficult to allocate goodwill as an asset to strictly defined industries in the context of the broader economic activity. This resource is not homogeneous in terms of internal structure, which could be regarded as a characteristic feature of the industry. From the economic sense and substance of goodwill it can be concluded that it is the amount 'accompanying' the occurrence of assets that are not recognized in the financial statements, but have a clear and often – significant – impact on the market value of the business entity, which is reflected in the agreed purchase price.

However, based on the literature one can point out studies, conducted in many countries, in which the relationship between the occurrence and percentage of goodwill in assets and industry was analysed. Strojek-Filus[8] (2013) had put for testing companies quoted on the Stock Exchange in Warsaw and companies from over-the-counter trading in years 2000-2010. Goodwill occurred primarily in the first group of companies. In the non-public companies, goodwill occurred very rarely and was less than 1% of value of total assets. A significant increase in the share of goodwill in the assets presented in the consolidated financial statements (from 0.19% in 2000 to 8.56% in 2010) occurred during the whole researched period. Based on the conducted studies the author has concluded that the consolidation goodwill appears most commonly in the Polish economic practice. Strojek-Filus also indicated industries in which goodwill accounted for the largest percentage of assets reported in the financial statements. These include: telecommunications (12.6%), hotels and restaurants (10.1%), electric machinery (9.5%), computer science (9.2%), food industry (7.8%) and utilities (7.1%). On the other hand the smallest proportion occurred in the energy sector (0.1%), fuel industry (0.4%) and plastics (0.7%).

The study also showed that goodwill most often occurred in the industries in which its share in the assets was the largest. The exception was the fuel industry with the highest percentage of companies with goodwill.

It is worth noting that the study by Glaume and Wyrwa (2011) on companies quoted on major European stock exchanges on the basis of the financial reports for 2009 showed that the highest average goodwill occurred in telecommunications, pharmaceutical, banking and media industries. The largest share of goodwill in assets occurred in the media, telecommunications, services, engineering industry (over 70%). Most of the results presented are consistent with the results obtained by Strojek-Filus for Polish companies. In light of the presented research results it can be concluded about the ‘sectorial‘ goodwill among companies quoted in public trading.

An industry particularly interesting from the point of view of goodwill is the media. This industry is ‘burdened’ with many derivatives of intangible assets that are not recognized in the statement of financial position, e.g. the trust of viewers, viewership, the system of celebrities gained to participate in programmes etc. The goodwill presented in the financial reports of selected companies quoted on the Stock Exchange in Warsaw for the years 2013 and 2014 was analysed for the purposes of this paper. Entities were selected in accordance with a key that demonstrated goodwill from the legal acquisition of other entity and goodwill on consolidation. The financial reports of two groups of companies from the media sector: TVN and Agora S.A. were compared in terms of the presence of goodwill on consolidation and explanations of this amount presented in the financial reports. Analysis of data disclosed in Wirtualna Polska S.A. reports was conducted in order to investigate verifiability and understandability of data provided on legal acquisition.

Case 1: Media group TVN S.A.

In 2014, the Parent Company TVN was controlled by the International Trading and Investments Holding based in Luxembourg. In 2015, the Group was subject to further ownership changes. In the report there is no clear presentation of the group structure with a clear indication of the percentage of subsidiaries, fellow subsidiaries and associates.

The basic data on the goodwill shown in the consolidated financial report for 2014 and 2013 are presented in Table 1 and 2.

[8] Detailed results of research on the determinants of prevalence of goodwill the author presented in the book entitled ‘Determinanty oraz skutki wynikowo-bilansowe identyfikacji i rozliczania wartości firmy w grupie kapitałowej’(*Determinants and balance sheet effects of identification and accounting of goodwill in the group*), Katowice: Wydawnictwo Uniwersytetu Ekonomicznego w Katowicach, 2013.

Table 1: Data on goodwill in the consolidated financial report

Year	Total assets in thou. PLN	Net profit in thou. PLN	Goodwill on consolidation in thou. PLN	Goodwill in investments in subsidiaries in thou. PLN	Impairment of goodwill on consolidation in thou. PLN
2014	3 814 767	189 350	144 127	434 959	0
2013	3 899 259	- 206 881	144 127	409 040	25 973

Table 2: Additional information on goodwill in the consolidated financial report

Year	Accounting policy on determining goodwill	The method of non-controlling interest valuation	Recognised goodwill included in investments under the equity method	Cash generating units	The adopted baseline test for goodwill impairment
2014	The formula for determining the goodwill according to IAS/IFRS	Does not refer	yes	yes	No data
2013	The formula for determining the goodwill according to IAS/IFRS	yes	yes	yes	No data

The goodwill is shown in the consolidated statement of financial position as a consolidation difference, which is a separate reporting item in the amount of PLN 144 127 thousand in the consecutive years 2013 and 2014. Financial report contains information about the acquisition of shares in the STAWKA Company on 16 October 2014 by the group. Buying more shares led to the loss of non-controlling interests. The report does not contain information on the conditions of the transaction (the amount paid, the fair value of net assets STAWKA Company, accounting policies used in the valuation of the company's assets at fair value). The consolidated statement of financial position shows that the company's value has not changed since 2013 and so the goodwill as a result of this transaction.

Moreover, the report also demonstrates the goodwill included in investments in associates valued by the equity method (note 26), broken down by:

— net assets,

— goodwill, and

— the carrying value of the investment.

The report gives the information on the conducted goodwill impairment test that confirmed the retention of the current value in 2014, although the allowance of PLN 25 973 thousand was carried out in 2013 due to the impairment of the cash-generating unit – teleshopping centre. The report for 2014 indicated two cash-generating units:

- thematic TV channels,
- TV production unit.

There is no data on conducting a test on, e.g. an adopted detailed projection period, the changes in the real rate of free cash flow to firm and the discount rate.

The disclosure concerning the correction of the goodwill calculation in investments in nC+ associate is given in note 26. It is indicated as a reason for the adjustment to recognize an additional provision in the amount of PLN 20 972 thousand and reduction of deferred tax asset. Therefore, the Group's share in the net assets of nC+ decreased by PLN 6 923 thousand, and goodwill increased by that amount. There is no value given after the adjustment.

In authors' opinion, the information disclosed by Media Group TVN is not clear and not sufficient enough in order to serve as a basis for the proper economic evaluation of goodwill included among other assets that are to generate future economic benefits. Because of the above, users of financial reports should pay special attention to the 2014 financial results that are considerably worsen when compared to previous years' financial profits.

Case 2: Media group AGORA S.A.

Agora Group consists of 16 subsidiaries, 5 jointly controlled and associates accounted for by the means of the equity method and 2 non-consolidated companies (including one in liquidation).

The basic data on the goodwill presented in the consolidated financial report for 2014 and 2013 is shown in Table 3 and 4.

Table 3: Data on goodwill in the consolidated financial report

Year	Total assets in thou. PLN	Net profit In thou. PLN	Goodwill on consolidation in thou. PLN	Goodwill in investments in subsidiaries in thou. PLN	Goodwill impairment on consolidation in thou. PLN
2014	1 556 499	- 11 026	311 104	No data	63 265
2013	1 642 857	1 179	374 369	No data	0

Table 4: Additional information on goodwill in the consolidated financial report

Year	Accounting policy on determining goodwill	The method of non-controlling interest valuation	Recognised goodwill included in investments under the equity method	Cash generating units	The adopted baseline test for goodwill impairment
2014	The formula for determining the goodwill according to IAS/IFRS	yes	No data	yes	yes
2013	The formula for determining the goodwill according to IAS/IFRS	yes	No data	yes	yes

Goodwill occurs as a consolidation difference, which is a separate item in the statement of financial position reports and – in the context of the equity method application by the group – as a component of the value of shares measured by this method. In the explanatory notes there are no figures about how to determine the goodwill, although the adopted method of valuation of non-controlling interests is indicated. In 2014, there was a strengthening of control in Helios S.A., Ad Taily Sp. z o.o., Sport4People Sp. z o. o, Sir Local Sp. z o. o. subsidiaries by taking up the newly issued shares (Consolidated Financial Report of Agora, 2014, pp. 62-64). There is no data on adopted solutions in the determination of fair value of net assets of subsidiaries and determining the difference of consolidation. The report introduces no explanation (figures) on goodwill included in the value of investments for valuation using the equity method. This also applies to the transaction of acquisition of shares in order to strengthen a significant impact on associates.

In the note explaining the goodwill as the consolidation difference, there are presented centres generating future cash flows broken down by:

- Internet,
- newspapers and magazines,
- radio activity,
- outdoor advertising segment,
- market for film screening ,
- sport4people.

There is also given a detailed projection period of 5 years to the test for goodwill impairment. The real rate of changes in free cash flow to firm and the discount rate before tax are also indicated for this period. There is no explanation provided for the adopted amounts.
The information provided is necessary to verify goodwill for making a possible write-off of goodwill impairment. In addition to the data, there are no explanations and calculations of the test for the impairment write-off made in 2014. From the complementary report on the consolidated financial reports emerges that the write-off due to the goodwill impairment in part

refers to two monthly magazines. The remaining amount of the write-off is not explained as to the cause.

The report on the activities of the Group Management Board of Agora S.A. for 2014 to the consolidated financial reports includes general information about testing for the impairment of assets (Consolidated Financial Report of Agora, 2014, p. 50)]. There are no more details.

The data published in the report on the formation of the consolidation difference or lack thereof at strengthening controls is not sufficient for a proper evaluation of this asset of the group. Although information on the carried out write-off contains required key figures by IAS/IFRS, but it does not allow the verification of the amounts shown. There is also no clear and transparent indication of the reasons for the write-off.

Case 3: Media group Wirtualna Polska Holding S.A.

In 2014 Wirtualna Polska Group encompassed 13 subsidiaries. On 1 October 2014 a legal merger followed on an acquisition of Wirtualna Polska S.A. that was subject to division into two organized parts. The Group decided that assets and liabilities separated from Wirtualna Polska S.A. constituted a business and were legally merged into the acquirer. A business merged constitutes the integrated set that is capable of being conducted and managed as a business because the department of editorial and advertising activities was separated leaving e-Commerce Centre within existing Wirtualna Polska S.A.

The purchase price paid for Wirtualna Polska S.A. amounted for PLN 382 498 thousand and included no contingent consideration. With reference to the acquisition of Wirtualna Polska S.A., the Group concluded a loan agreement and it was granted loans in total amount up to PLN 270 million, of which PLN 175 million was dedicated for the purchase of Wirtualna Polska S.A. The remaining part of the consideration transferred was financed in the form of a capital increase.

The acquisition method was used in order to account for a business combination and positive goodwill was disclosed in financial report. According to data presented in financial report, goodwill relates to a cash-generating unit encompassing trademark “WP.pl”. Trademark with unlimited time of life was valued at PLN 102 500 thousand. The basic data on the goodwill presented in the consolidated financial report for 2014 is shown in Table 5.

Table 5: Data on goodwill in the consolidated financial report

Year	Total assets in thou. PLN	Net profit in thou. PLN	Goodwill in thou. PLN	Goodwill from business combination in thou. PLN	Goodwill impairment in thou. PLN
31.12.2014	569 820	4 149	124 833	92 028	0

The amount of goodwill presented in financial reports was allocated to 4 different cash-generating units based on IAS/IFRS requirements. The largest one is Wirtualna Polska S.A. arising from the legal acquisition described above. The entity presents detailed information about the assets and liabilities’ acquisition-date fair values. Summary of disclosed information is presented in Table 6.

Table 6: Additional information about goodwill calculations

Item	**In thou. PLN**
Consideration transferred in the acquisition	**382 498**
Cash and cash equivalents	5 659
Fixed assets	44 392
Trademarks	102 500
Website and WP.pl emails	152 300
Copyrights and other intangible assets	7 699
Trade receivables	31 519
Other current assets	27 661
Trade liabilities	(32 345)
Loans	(477)
Provisions and contingent liabilities	(2 872)
Deferred tax liabilities	(45 566)
Net assets acquired (in total)	290 470
Goodwill	92 028

Additional to the information presented in the Table 6, the reporting entity informs that the costs of the acquisition amounted for PLN 12 645 thousand and the indicated value was expensed in the profit and loss in 2013 and 2014.

Goodwill was subject to an impairment test as at 31 December 2014. Recoverable amount of cash-generating unit was based on the calculations of value in use. Basic assumptions that are material to the assessments made include annual revenue increase ratio and discount rate used in calculating the values. Cash flow projects were prepared based on the 2015 budget, as well as past financial results and managements' plans. There is no information regarding specific amounts of revenue increase ratio used, except for a ratio used for residual period beyond the five-year forecast period, at the level of National Bank of Poland inflation target of 2,5%. Discount ratio was estimated using available macroeconomic and market data and it amounts 10,1%.

DISCUSSION

Goodwill is – inherently – an asset much more difficult to assess correctly and accurately than other assets. Its economic sense is based on a proper assessment of other resources not recognized in the statement of financial position. Therefore, it requires special care and detail in the presentation of the reporting and explanatory notes.

The analysis of selected cases showed that disclosures related to acquired goodwill presented in the financial reports are not sufficient to assess and correctly interpret this asset of an entity and group. Great flexibility in a way and scope of information disclosure is noteworthy, particularly concerning the original determination of goodwill and impairment testing of its value. Data on the solutions adopted in determining the fair value of net assets and the determination of non-controlling interests is essential in this case. This discretion also applies to data on the size of the base adopted for the cash-generating units. Despite formal complying with the requirements of IFRS 12 on additional disclosures regarding goodwill in affiliates, the amount is still difficult to interpret. There is no justification for taken baselines if they are given in the report.

Conceptual framework states that verifiability helps assure that information faithfully represents the economic phenomena it purports to represent. Verifiability means that different knowledgeable and independent observers could reach consensus, although not necessarily complete agreement, that a particular depiction is a faithful representation. Based on our findings it can be stated that goodwill financial reports' disclosure does not provide required information in order to achieve verifiability in the case of 3 analysed entities. It is not possible to conduct neither direct nor indirect verification, because users of financial statements do not have any detailed information about input data, formulas or techniques used in order to recalculate the outputs using the same technology. Moreover, underlying assumption relating to the future as well as methods of compiling the information was not disclosed.

Given that goodwill is usually a significant part of the total purchase price and important element of assets, users of financial reports might require a quantitative, and – what is more important – detailed qualitative description classifying, characterizing and presenting information clearly in order to make is understandable. Failure to comply with international standards and conceptual framework requirements might lead to the situation when asset recognition criteria are not met. The observation made from the analysis shows that entities do little more than repeat the wordings from IAS/IFRS. This practice does not ensure high quality of financial reports. Furthermore, the information about the components of goodwill is omitted, and mathematical calculation is emphasized prioritizing the residual character of goodwill. Unverifiable estimates resulting in goodwill measurement and amount of impairment loss result in decrease in reliability. Subjectivity embedded in the application of mathematical formulas threatens the relevance of disclosed information. On the other hand, subjectivity and hard-to-verify assumptions call for valuation expertize done by independent professionals.

Our findings are consistent with Ding, Richard, Stalowy (2008) research pointing out that accounting treatment for goodwill presents the shift from a stakeholder model to shareholder model, which leads to the preference for short-term rather long-term profit. The move to actuarial solution was judged by the assumption that financial reports should provide data more close to market values, and therefore more useful to investors. The observation of no impairment write-offs even the acquired operations have declined, stands for the short-term demand for dividends. Also Z. Krizova, J. Sedlacek, and E. Hyblova (2012) conducted an analysis of goodwill disclosure made by Czech enterprises and obtained similar results pointing out that companies fail to comply with simple disclosure requirements. In like manner C. Lee (2011) summarizes his findings concentrated on the ability of goodwill to predict future cash flows. In his article Lee pinpoints the subjectivity of assumptions underlying goodwill measurements.

The presented issues related to the reporting of goodwill translate into additional requirements for the educational process in this regard. The student should possess the ability not only to calculate the goodwill correctly, but also to recognize and interpret areas of intentional treatment of this asset from the point of view of building the image of the financial situation of the entity and the group. Ethical attitudes to the valuation of assets and liabilities are becoming of particular importance, which requires the introduction of moderated discussion to the educational process on a wider-scale and analysis of case studies on different variants of actions taken by accountants and managers. The student should be sensitive to the fact that, in case of presenting goodwill in the financial report, lack of information or incomplete information can mean the inability of its proper assessment. In case of a significant share of goodwill in assets it could mean the inability to assess correctly the financial position of the entity.

CONCLUSIONS

The history of accounting for goodwill shows that there seems to be no simple way of correcting the contemporary issues referring to accounting for goodwill. It seems that the developed solutions created more difficulties than they solve. Financial information presented by publicly traded companies affects the functioning of capital market, and earnings influence incentives and decisions regarding directions of investments of scare economic resources. Thus, economists have a real problem to solve in order to ensure that financial reports reflect a realistic economic picture of a business entity. As accounting disclosure should be neutral in presenting the economic facts, ambiguity of choices in financial calculations and presentation shall be limited to achieve the neutrality. Alternatives are available in the area of goodwill valuation and presentation, but the choice of one or the other may produce substantially different results in the statement of financial position and in the statement of comprehensive income. Moreover, comparability of financial statements, elements of assets, liabilities and equity is deteriorated.

To overcome abuses, the creation of precise regulation might not be enough. The willingness by companies to disclose unbiased and understandable information is a must. Because the existence and the value of goodwill mainly depends on the circumstances of the transaction of business combination, accountants should present the economic nature of goodwill proving that the item meets the requirement of an asset, especially regarding its nature and faithful representation of economic phenomena of business combination conducted. The complex nature of economic resources incorporated in the goodwill oblige for broad disclosures and fair explanations. Accountants' awareness is also important in the years following the first valuation of goodwill. Measurement of goodwill done at the time of business combination loses its validity due to the changes in economic situation on the market, strategic decisions made within a company or other variables included in the initial valuation. In order to assure the high quality of economic information delivered by goodwill position disclosed in financial reports during the years following business combinations, financial disclosure referring to changes of estimates and detailed data referring to cash generating units is desired. As goodwill is inseparable to assets of the acquired entity, the information about the cash-generating unit (including changes in revenue and profitability) shall be delivered in order to capture the intangible dimension of the entity. Summarizing, the conducted research suggests that the most important information is missing in financial reports of Polish publicly traded companies: the description of the economic nature of goodwill purchased and the changes in the forecasted economic benefits arising from cash generating unit encompassed in the goodwill.

In authors' opinion, there is a need for more fundamental approach to goodwill instead of arithmetical pursuit mostly manifested in the accounting literature and practice. The change in goodwill presentation would represent a major change in analytical-mathematical bookkeeping, which could have a serious positive impact on the quality of information disclosed in financial reports. Stressing the importance of fundamental and conceptual approach to goodwill will not change any of accounting concepts, axioms or methods at the same time. Of course, there is no warrant for the proposal that all qualitative information would be of high quality securing that financial reports help users form appropriate perceptions concerning intangible dimension of the entity. The awareness of accountants to the need of enhanced disclosure shall be accompanied by ethical awareness referring to the importance of accounting information on the contemporary capital markets. It is not only about accountants, their ethics, knowledge and competences, but also about investors who attach different valuation weights to various goodwill components of accounting goodwill numbers.

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