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FINANCIAL REPORTING STANDARDS IMPLEMENTATION COMMITTEE

FRSIC Consensus 4

Accounting Treatment for Impairment of Goodwill in Situation where Court Approval has been obtained to write it off against Reserves

Introduction

FRSIC Consensus 4 "Accounting Treatment for Impairment of Goodwill in Situation where Court Approval has been obtained to write it off against Reserves" was developed by the Financial Reporting Standards Implementation Committee ("FRSIC") and issued by the Malaysian Institute of Accountants ("MIA" or "Institute") on 27 March 2008.

The Consensus contained herein is issued as part of the Institute's initiatives to promote best practices in compliance with the highest standards in financial accounting.

FRSIC CONSENSUS 4**ACCOUNTING TREATMENT FOR IMPAIRMENT OF GOODWILL IN SITUATION WHERE COURT APPROVAL HAS BEEN OBTAINED TO WRITE IT OFF AGAINST RESERVES**

FRSIC Consensus is guidance issued by MIA and shall be regarded as best practice. It should be read in conjunction with the respective applicable accounting standards.

Members of MIA are expected to observe compliance to the consensus issued. In exceptional circumstances where departure is necessary, members shall be prepared to justify the departure.

FRSIC Consensus need not be applied to immaterial items. Nothing in the FRSIC Consensus is to be construed as amending or overriding the accounting standards or other statements adopted or issued by the MASB and other relevant laws.

Background

1. With effect from 1 January 2006, companies are required under FRS 3, Business Combinations ("FRS 3"), to recognise goodwill acquired in a business combination as an asset and test the goodwill for impairment annually. Any impairment loss is to be recognised as an expense in the income statement immediately as required by paragraph 60 of FRS 136, Impairment of Assets ("FRS 136").
2. The requirement of FRS 136 for impairment loss to be recognised as an expense in the income statement is no different from that required by its predecessor, FRS 136₂₀₀₄, Impairment of Assets, which came into effect on 1 January 2002.
3. Section 64 of the Companies Act, 1965 provides the court with power to allow companies to reduce their share capital and share premium. However, the court approval does not specify the manner in which the reductions are to be effected in the financial statements.

4. In the past, certain companies have obtained High Court approval pursuant to Section 64 of the Companies Act, 1965 and had written off goodwill directly against reserves (e.g. share premium reserve).

The Issue

5. The issue is whether the past practice of writing off the goodwill directly against reserves based on a high court approval is in accordance with the requirements of Financial Reporting Standards.

Consensus and Basis of Consensus

6. Paragraph 60 of FRS 136 requires that an impairment loss to be recognized immediately in profit or loss.
7. Paragraph 78 of FRS 101, Presentation of Financial Statements ("FRS 101") requires all items of income and expenses recognised in a period shall be included in profit or loss unless a Standard or an Interpretation requires otherwise.
8. However, currently, there is no Standard that permits impairment of goodwill to be written off directly against reserve without going through the income statement.
9. Based on the above, the Committee concluded that any impairment of goodwill should be recognised immediately in profit or loss as required by FRS 136 and FRS 101 and not be written off directly to reserves.
10. The amount of impairment loss included in the retained earnings may then be transferred from retained earnings to reduce share premium account pursuant to Section 64 of the Companies Act, 1965 as sanctioned by a High Court approval.

Issuance Date of this Consensus

11. This Consensus is issued on March 27, 2008.

References

FRS 3 "Business Combination"

FRS 101 "Presentation of Financial Statements"

FRS 136 "Impairment of Assets"

Companies Act, 1965

[Malaysian Bar: 1210] Circular 293/2007: Issue of non-compliance of Financial Reporting Standards requirements when applying for Court Order for goodwill to be written off against reserves dated 19 December 2007.