

Is Amortization Good Enough? Evidence from the U.K. Goodwill Accounting

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ABSTRACT

Before 2001, the accounting practitioners generally amortize the cost of intangibles over an arbitrary decided period of time. The accounting treatment lies in two perspectives: first, the value of goodwill will eventually decline; second, the recognition of amortization expenses is to meet the requirement of matching principle. However, later research indicates that the value of goodwill does not necessarily fall afterwards, and may even increase under certain circumstances. 'Impairment Testing' is thus introduced to replace 'amortization' to reflect the true and fair view of assets values. However, impairment testing is liable to manipulation and may impose huge costs on firms, when they have frequent mergers and acquisitions activities. This paper empirically examine whether the old fashion way – amortization - of recognizing the depreciation of intangible assets can serve the function, given 'impairment testing' is costly and manipulative? The empirical evidence indicates positive answer to the above question.

INTRODUCTION

The FASB issued Statement of Financial Accounting Standards (SFAS) No. 141 – *Business Combinations* in 2001, which abolished the use of the pooling-of-interests method in recording a business combination. To avoid the resulting drag on reported earnings (recognition of goodwill amortisation charges for the subsequent years for up to 40 years under Accounting Principles Board (APB) opinion No. 17 – *Intangible Assets* (APB, 1970), the FASB also published the Statement of Financial Accounting Standards (SFAS) No. 142 – *Goodwill and Other Intangible Assets* to wipe out the need for amortisation, subject to a two-step process of impairment testing. One interesting phenomenon observed here is that while the UK standard-setter, the ASB, mandates companies to capitalise purchased goodwill and amortise it over its useful life (previously companies generally adopted the direct write-off method and did not recognise amortisation charges), the US counterpart has moved in the other direction, and abolished the amortisation charges entirely. In 1970, the US was the first country to require systematic amortisation of goodwill over an arbitrary maximum useful life of 40 years. 30 years later, it changed its regime to another extreme. So, why the change? Commentators suggest that the reason could be to avoid the recognition of the often large amortisation charges.

Amortisation causes concern because it takes a large proportion of profit from companies and also it affects the profits of subsequent periods. For example, in Vodafone AirTouch's 2000 accounts, the profit before amortisation charges is £1655 million. When the goodwill amortisation of £1712 million was deducted, a loss of £57 million was left. Thus the profit is totally wiped out by merely recognising the amortisation expenses of a quasi-asset that arguably does not really exist. In its 2002 (2001) accounts, the amortisation charges continue to exert a significant negative influence on earnings. According to press releases, the earnings before goodwill amortisation and exceptional items are £6199 (£4027) million, the earnings after goodwill amortisation and exceptional items are -£13539 million (the largest annual loss recorded in British corporate history) for 2002 and -£8086 million for 2001, where amortisation alone is £13470 and £11873 million for 2002 and 2001 respectively. France Telecom also wrote down €10.2 billion, KPN of the Netherlands €12.4 billion and Deutsche Telekom €15.2 billion (see *The Economist*, June 1st 2002).

Prior to FRS 10, UK companies were reluctant to adopt the capitalization method, with the need to amortize goodwill being one of the main factors contributing to this reluctance (Taib, 1996). After FRS 10, quite a few companies presented their earnings both before and after charging for amortization, and the same situation applied when SFAS No. 142 was still at draft stage (Johnson and Petrone, 2001). It could be argued that the 'dual-presentation' promotes investors' understanding of the components of earnings and also clears up confusion. Duvall et al. (1992)

discuss how arbitrary amortisation periods for goodwill, coupled with inadequate disclosure, make it difficult for investors to evaluate goodwill amortization information.

The recognition of amortization is an issue which led to the research question asked in this paper: does the value-relevance of goodwill diminish over time? Does amortization provide useful information for investors?

It is clear that the costs of implementing such an impairment test will be quite high. In a survey conducted by the American Business Conference, Grant Thornton, LLP, and the NASDAQ Stock Market, Inc. (Lewis et al., 2001), CFOs were asked about how they would handle the valuation provisions of SFAS 142. 57% of CFOs said that they would be likely or almost certain to use 'outside assistance' when attempting to value a reporting unit and its assets and liabilities, and 71% would use outside assistance when performing the impairment test. In addition to that, although companies will have higher reported earnings under SFAS 142, there will be no change in cash flows. Is all this worth the cost? There is no easy answer to this question. Both amortisation and impairment testing have a certain degree of subjectivity, and each have different shortcomings either in theoretical support or implementation difficulties. There is no perfect solution to satisfy everyone on the choices of how to report the decline in the value of goodwill.

MODELS AND HYPOTHESES

Many empirical tests (see for example, Jennings et al., 1996; Ibraham, 1999; Wang, 2002) suggest that investors view purchased goodwill as an asset. This paper now proceeds to test a number of additional hypotheses based on the finding above. It examines whether the value-relevance of goodwill declines with the age of the goodwill. In other words, does the market normally perceive goodwill as a wasting asset or as a non-wasting asset, the latter is the basic assumption under SFAS 142? Further, by reference to the impact of goodwill acquisitions on subsequent earnings, it looks for evidence of a suitable depreciation pattern. It explores whether the coefficients suggest a straight-line depreciating pattern, a reducing balance depreciating pattern, a non-zero depreciating pattern or whether there is no discernible evidence as to a depreciation pattern. Finally, it looks at whether the earnings figure without amortization is more value-relevant than the earnings figure with amortization.

Previous literature has suggested that if goodwill is a wasting asset, amortisation is chosen to reflect the expected pattern of diminution of the goodwill. On the other hand, if goodwill is not generally a wasting asset, i.e., its value does not decline over time, pre-determined amortisation is not appropriate in this case. However, as the modern business features a high rate of technology advance and high competitiveness, it is hardly convincing that the value of goodwill can be maintained infinitely. Therefore, periodical impairment testing will be needed to monitor whether the value of goodwill diminishes. This might provide some justification for the use of impairment tests.

Empirical evidence either showed that goodwill is a non-depleting asset (Henning et al., 2000), or that the association between market value and amortisation expenses is weak (Duval et al., 1992; Jennings et al., 1996; Ibrahim et al., 1999; Lindenberg and Ross, 1999). These results seem to suggest that predetermined amortisation is not capable of truthfully representing the impairment in the value of goodwill. Impairment testing, which is expected to review the fair value and carrying value of goodwill periodically, may have the potential to better represent the economic substance of purchased goodwill in this regard. Based on prior research, I aim to examine whether goodwill depreciates over time, the hypothesis is thus developed as follows:

H₁: The Value-Relevance of Goodwill Is not Associated with the Age of Goodwill.

I regressed market value on lagged acquired goodwill of different ages to test the association between the value-relevance of goodwill and the changes in goodwill for each year during 1993 – 1999. The explanatory variables thus comprise goodwill of different ages. This research design is seeking to observe whether there is a pattern of decline in the total expected future payoffs from goodwill. As the goodwill gets older, if the coefficients of changes in cumulative goodwill do not decline over time, after controlling for other variables, then the null hypothesis will be accepted. In this case, the results would provide no evidence that the market perceives goodwill as a wasting asset. This would suggest some support for the non-amortization/impairment testing only approach. On the other hand, if the coefficients decline with the age of goodwill, it is then perceived as a depleting asset. Amortisation charges, either by systematic amortisation or by impairment tests, are expected to represent its diminution in value. The study intended to take one step further to derive an approximate economic amortisation rate, if any, from the pattern of decrease in the coefficients.

In addition to the above research design, I also look into the impact of goodwill acquisitions on earnings. The rationale is that assets are expected to bring future cash inflows to companies. Therefore, a relationship between operating profits and assets is established (see Lev and Sougiannis). Based on this concept, the second test regresses operating profits on lagged acquired goodwill of different ages in each year during 1993 – 1999 (the age of goodwill). Goodwill is perceived as an asset, hence the benefits it brings are expected to be realised in the earnings. I expect to observe the periodic realisation of profits from goodwill (by a significant and positive relation to operating profits), and the life span of goodwill (how long does the goodwill remain significant, i.e., the empirical amortisation period) in this regression. The coefficients on various age of goodwill represent the benefits from goodwill realised in the form of earnings. The sum of these coefficients equals the total benefits that goodwill brings to the current earnings. In the event that I observe a declining pattern (a straight-line declining pattern or reducing-balance declining pattern), an empirical amortisation rate could potentially be derived from the ratio of each individual year's benefit over total benefits (Lev and Sougiannis, 1996).

Jennings et al (2001) and Moehrl et al. (2001) have both reached the same conclusion that goodwill amortization disclosures are not decision-useful, and therefore they support the non-amortization/impairment testing only approach. I thus follow Jennings' work by carrying out a further test on UK data to examine whether amortisation is value-relevant in explaining the variation in share prices, i.e., are earnings before or after the amortisation charge more useful in explaining market value? The hypothesis is then set up as follows:

H₂: Earnings before Amortisation Are not More Value- Relevant than Earnings after Amortisation.

RESEARCH DESIGN AND DATA DESCRIPTION

The Association Between the Market Value and the Changes in Goodwill

To test the hypothesis specified in the previous section, whether goodwill is a non-wasting asset, I employed two research designs to provide empirical evidence. The first research design is derived from the regression used in Wang (2002), except that I slice cumulative goodwill by age. I then examine the correspondence between market value of equity and various lags of goodwill changes. Specifically, this is done by observing the association between a number of lagged goodwill items and the market value from the following regression, for t = 1993 to 1999:

$$MV_{i,t} = \alpha_{0,t} + \alpha_{1,t}NBV_{i,t} + \alpha_{2,t}EARN_{i,t} + \sum_k \alpha_{3,k,t}CCGW_{i,t-k} + \alpha_{4,t}SIZE_{i,t} + \varepsilon_{i,t} \quad (1)$$

where,

$MV_{i,t}$ = the market value of common stock measured 4 months after the end of the current fiscal year for firm i, (DSMV)

$NBV_{i,t}$ = book value of equity exclusive of any goodwill included therein, (DS1107 – DS306 – capitalised goodwill)

$EARN_{i,t}$ = net profit from continuing operations before goodwill amortisation expenses for firm i, (DS625 + amortisation charges)

$CCGW_{i,t-k}$ = this is the cumulative goodwill number that appears on the Balance Sheet. It is now broken down by age (i.e. length of time since acquisition). The sum of these components of different age should be equal to the cumulative goodwill balance. k is the various lags of cumulative goodwill from 1993 – 1999.

$SIZE_{i,t}$ = the logarithm of sales.

All the variables in regression (1) (except the control variable, $SIZE$) are deflated by a variety of scaling variables, total assets at the beginning of the year (exclusive of capitalised goodwill), market value of equity at the beginning of the year, and book value of equity at the beginning of the year (exclusive of cumulative goodwill) separately. This is to mitigate problems associated with 'scale effects' and heteroscedasticity.

By observing the trend of the coefficients on goodwill ($\alpha_{3,0}, \alpha_{3,1}, \alpha_{3,2}$... etc), the study provides evidence to test whether goodwill is a wasting asset. If goodwill is perceived by the market as a wasting asset, the study expects a negative association between the magnitude of the coefficients on the tranche of goodwill and the age (k) of the tranche

of goodwill, since the contribution/impact of the purchased goodwill to the market value decreases as time goes by. On the other hand, if investors view goodwill as a non-wasting asset, the coefficients on the various tranches of goodwill should not decline with the passage of time.

If the value of purchased goodwill does decline over time, the rate of decline in the coefficients on goodwill provides a basis for estimation of the appropriate amortisation rates for goodwill. Specifically, if investors perceive goodwill as a non-depleting asset, I expect the coefficients on the various lags of cumulative goodwill, i.e., $\sum_k \alpha_3 CCGW_{i,t-k}$, to stay significant and maintain a non-declining pattern over the passage of time. On the other hand, if the evidence shows that goodwill is viewed as a depleting asset, I expect to observe a declining pattern (a straight-line declining pattern or reducing-balance declining pattern) on the changes in cumulative goodwill. The test could then go one step further potentially to calculate from the declining pattern to derive the empirical /economic amortisation rates (the rates may be different from the rates stipulated by various standard-setters).

It should be noted that in regression (1), market value impounds all expected periodic flows. If goodwill is a non-wasting asset, the coefficients on the various lags of goodwill are also expected to remain significant indefinitely.

The Association Between the Operating Profit and the Changes in Goodwill

The second research design is related to the one used in Lev and Sougiannis (1996). It examines the association between earnings and various ages of goodwill expenditures. Lev and Sougiannis used this method as a basis to estimate the amortisation rates for R&D expenditures. In their study, the estimation procedure started by regressing operating income on lagged R&D expenditures and other control variables over the period of 1975 – 1981. The coefficients of R&D expenditures are interpreted as the contribution of a dollar of R&D expenditure to subsequent earnings. They then used these coefficients to estimate amortisation rates. My second regression is structured as follows to estimate the contribution of goodwill as an asset to the earnings, 1993 – 1999:

$$OP_{i,t} = \beta_{0,t} + \beta_{1,t}TA_{i,t} + \sum_k \beta_{2,k,t}CCGW_{i,t-k} + \varepsilon_{i,t} \quad (2)$$

where, $OP_{i,t}$ = net profit from continuing operations before amortisation expenses for firm i in year t, (DS625 + amortisation charges)

$TA_{i,t}$ = book value of total assets after excluding goodwill numbers, (DS392 + CGW)

$CCGW_{i,t-k}$ = the change in cumulative goodwill original cost, i.e., goodwill on acquisition in each year. This variable includes companies that wrote off goodwill to reserves, that capitalised before FRS 10, and that capitalised under FRS

10. k is the various lags of cumulative goodwill from 1993 – 1999.

Both dependent and independent variables are scaled by total sales (DS104) to avoid heteroscedasticity problems.

My focus in regression (2) is to observe whether there is any measurable connection between goodwill acquisition and subsequent earnings, and any further evidence that the earnings impact of acquired goodwill ceases after a period of time. In particular, over how long a period do the various coefficients on $\sum_k \beta_{2,k,t}CCGW_{i,t-k}$ maintain their

significance, i.e., what is the span of goodwill's life? In regression (2), since profit is a periodic flow, the effect of a particular item of acquired goodwill on earnings is expected eventually to die out.

EMPIRICAL RESULTS

The sample size are originally 7965 firm-year observations from DATASTREAM. After deducting missing operating profits data, the observations became 7412. I then trimmed the sample by removing 1% the most extreme values (in absolute value) from the medians. The final sample size for the operating profit model is 7248. (untabulated)

Table 1 presents the regression results from market value on various lags of changes in cumulative goodwill. The focus in this test is on the coefficients on various lags of goodwill, i.e., $\alpha_{3,0}$, $\alpha_{3,1}$, $\alpha_{3,2}$, $\alpha_{3,3}$, $\alpha_{3,4}$, and $\alpha_{3,5}$. Visual inspection of the results indicates that the value-relevance of goodwill remains significant over time, but the coefficients are comparatively small and that there is no clear pattern of fluctuation (increase, maintain, or decrease) in value. Hence there is no conclusive evidence here showing that goodwill is or is not a wasting asset, or that an empirical amortisation rate is obtainable. Table 1 shows goodwill acquired in 1994 remains significant (at the 1% level) over the period from 1994 to 1999. That is, in 1999, the goodwill is broken down to 6 components: goodwill acquired in 1994, 1995, 1996, 1997, 1998 and. The coefficients (t-statistics) for these 6 parts of goodwill in 1999 are 2.12 (4.50), 3.51 (3.59), 1.61 (1.58), 1.97 (2.58), 2.73 (3.39), and 1.78 (2.34) for the years chronologically. All statistics are significant at the 5%. Similarly, in 1998, goodwill contains that acquired in 1994, 1995, 1996, 1997, and 1998. The coefficients (t-statistics) for these 5 parts are: 1.75 (11.31), 2.69 (6.76), 2.02 (5.99), 1.98 (6.72) and 2.39 (9.00) separately. All statistics are significant at the 1% level. Taken together, the results in Table 1 suggest that the value-relevance of goodwill exists not only at the time of acquisition but also persists in the subsequent years – in this study, from 1994 to 1999. However, no regular pattern of movements in the coefficients. If there is diminution in the value of goodwill over time, it does not occur in the systematic manner that periodic amortisation suggests.

Table 1: Coefficient Estimates of Market Value Regressed on Various Lags of Changes in Cumulative Goodwill

$$MV_{i,t} = \alpha_0 + \alpha_1 NBV_{i,t} + \alpha_2 EARN_{i,t} + \sum_k \alpha_{3,k} CCGW_{i,t-k} + \alpha_4 SIZE_{i,t} + \varepsilon_{i,t} \quad (\text{Scaled by Beginning Book Value})$$

Year	Obs	α_0	α_1	α_2	$\alpha_{3,0}$	$\alpha_{3,1}$	$\alpha_{3,2}$	$\alpha_{3,3}$	$\alpha_{3,4}$	$\alpha_{3,5}$	α_4	Adj- R^2
1994	618	1.39 (1.83)	1.38*** (6.14)	4.44*** (12.00)	0.76*** (11.66)	–	–	–	–	–	-0.07 (-1.20)	0.45
1995	542	0.52 (0.51)	1.82*** (5.42)	3.78*** (7.55)	1.04*** (5.59)	0.94*** (9.75)	–	–	–	–	-0.02 (-0.25)	0.34
1996	504	-0.94 (-0.75)	2.29*** (5.47)	6.01*** (7.94)	1.15*** (5.05)	2.15*** (8.42)	1.06*** (8.09)	–	–	–	0.03 (0.29)	0.50
1997	439	-2.26* (-1.78)	2.48*** (5.76)	3.48*** (4.91)	1.31*** (5.14)	1.55*** (5.09)	2.57*** (7.61)	1.62*** (12.20)	–	–	0.13 (1.20)	0.43
1998	385	-1.66 (-1.12)	2.09*** (3.66)	3.05*** (5.07)	2.39*** (9.00)	1.98*** (6.72)	2.02*** (5.99)	2.69*** (6.76)	1.75*** (11.31)	–	0.08 (0.70)	0.47
1999	273	-2.88 (-0.93)	3.31*** (2.58)	4.42*** (2.94)	1.78** (2.34)	2.73*** (3.39)	1.97*** (2.58)	1.61** (1.58)	3.51*** (3.59)	2.12*** (4.50)	0.10 (0.44)	0.25

*significant at the 10% level **significant at the 5% level ***significant at the 1% level

Variables are defined as follows: $MV_{i,t}$ = the market value of common stock measured 4 months after the end of the current fiscal year for firm i, (DSMV); $NBV_{i,t}$ = book value of equity exclusive of any goodwill included therein, (DS1107 – DS306 – capitalised goodwill); $EARN_{i,t}$ = net profit from continuing operations before goodwill amortisation expenses for firm i, (DS625 + amortisation charges); $CCGW_{i,t-k}$ = this is the cumulative goodwill number that appears on the Balance Sheet. It is now broken down by age (i.e. length of time since acquisition). The sum of these components of different age should be equal to the cumulative goodwill

The results of applying the second research design, $OP_{i,t} = \beta_0 + \beta_1 TA_{i,t} + \sum_k \beta_{2,k} CCGW_{i,t-k} + \varepsilon_{i,t}$ is

presented in Table 2. It exhibits the impact of various lags of goodwill on operating profits. Generally, the goodwill acquired in the current period has insignificant impact on current earnings during the period of 1993 – 1999. The goodwill from acquisitions in current year is largely statistically significant but the impact on earnings is very low and near zero. Most of the years did not show a constant realisation in profits over the sample period. Put together, the results suggest that the market perceives purchased goodwill as an asset from regression (1), where market value impounds all expected periodic flows. However, the relationship between goodwill and subsequent earnings is not very evident. It shows no consistent pattern of effects of purchased goodwill on operating profits, although in some cases benefits remain significant over the next two or three years. Since there is no apparent pattern (straight-line declining,

reducing balance declining, or non-declining) of depreciation on various lags of goodwill, I therefore did not estimate an empirical amortisation rate from regression (2). In summary, these results are inconclusive. They are not able to suggest whether impairment tests or arbitrary amortisation is more appropriate to reflect the decline in the value of goodwill.

Table 2: Coefficient Estimates of Operating Profits Regressed on Various Lags of Changes in Cumulative Goodwill

$$OP_{i,t} = \beta_0 + \beta_1 TA_{i,t} + \sum_k \beta_{2,k} CCGW_{i,t-k} + \varepsilon_{i,t} \text{ (Scaled by Sales)}$$

Year	Obs	β_0	β_1	$\beta_{2,0}$	$\beta_{2,1}$	$\beta_{2,2}$	$\beta_{2,3}$	$\beta_{2,4}$	$\beta_{2,5}$	$\beta_{2,6}$	Adj-R ²
1993	852	0.06*** (7.07)	-0.01** (-2.15)	0.07** (2.35)	–	–	–	–	–	–	0.01
1994	793	0.05*** (9.66)	0.03*** (7.72)	0.21*** (6.65)	0.04** (2.36)	–	–	–	–	–	0.10
1995	742	0.04*** (7.49)	0.04*** (9.84)	0.11*** (2.94)	0.12*** (3.62)	0.06*** (3.43)	–	–	–	–	0.13
1996	684	0.08*** (8.67)	-0.01 (-0.96)	0.25*** (3.91)	-0.03 (-0.46)	0.03 (0.58)	-0.04 (-1.24)	–	–	–	0.02
1997	619	0.05*** (6.01)	0.02*** (3.33)	0.21*** (2.74)	0.19*** (2.94)	0.01 (0.20)	0.02 (0.31)	0.01 (0.32)	–	–	0.04
1998	535	0.11*** (9.77)	0.07*** (-10.13)	0.03 (0.44)	0.07 (0.70)	0.29*** (3.43)	-0.05 (-0.79)	-0.08 (-1.01)	0.04 (1.20)	–	0.19
1999	432	0.05*** (5.97)	0.01** (2.17)	0.14*** (2.61)	0.08 (1.62)	0.16** (1.90)	0.12** (1.94)	0.08 (1.52)	-0.03 (-0.45)	0.04 (1.38)	0.05

*significant at the 10% level **significant at the 5% level ***significant at the 1% level

OP is operating profit.

TA is the total assets exclusive of cumulative goodwill.

CGW is the cumulative goodwill number constructed by this study.

CONCLUSIONS

SFAS No. 142 assumes goodwill is a non-wasting asset, hence no amortisation is required. I test the assertion that goodwill is a non-depleting asset by looking at the association between market value and various ages of goodwill. I also examine how the goodwill acquisition affects future earnings, and observe how long a period the impact lasts. Furthermore, I test whether financial statement users regard goodwill amortization expense as useful information in analysing investments.

The results of tests on the association between market value and various age of goodwill show that goodwill keeps its value-relevance over a period of time. However, the coefficients of goodwill at various ages have insignificant impact on market value. Thus it is difficult to conclude whether goodwill is a non-wasting asset or not. Moreover, I cannot find a clear pattern of decline in value (straight-line declining, reducing balance declining or zero depreciation) in the coefficients of changes in goodwill from regression (1). This might suggest that it may seem arbitrary to allocate the cost of goodwill over a predetermined useful life. The two-step impairment test may be better in deciding the impairment loss in the value of goodwill.

The results from regression (2) suggest that various ages of goodwill do not have significant impact on current earnings. As with the results shown in regression (1), I did not observe a clear pattern of depreciation of goodwill in regression (2), therefore, I did not proceed to estimate an empirical amortisation rate for goodwill. Taken together, my empirical results from regressions (1) and (2) indicate that market value is associated with various ages of goodwill, and remains significant over the whole sample period, but that the relationship between various ages of goodwill and subsequent earnings is rather weak. The results do not provide strong evidence to support the claim that goodwill is a non-wasting asset nor can it support that impairment testing is preferred to arbitrary amortization.

In summary, the results presented in this paper show weak evidence as to whether goodwill is a wasting asset or not. However, the implication from the results may be able to shed some light on the arguments of backing from impairment testing to systematic amortization. SFAS 142 mandates companies to adopt a non-amortization/impairment testing only approach to account for the diminution in the value of goodwill. The AcBS follows this approach, the IASB and the AASB are also considering to follow this path. It seems impairment testing is currently the most favoured practice among the major jurisdictions in the world. The rationale behind this approach is that goodwill is a non-depleting asset, and arbitrary amortisation not only cannot reflect its real depreciation, but also distorts earnings. Impairment testing assesses the value of goodwill periodically, and hence it is expected to provide accounting information with a higher degree of relevance. However, considering the complicated procedures, the time lag in recognising its impairment in value and the subjective judgement involved in this approach, the information is also expected to be less reliable. Moreover, since managers are likely to recognise less amortisation charges to boost their earning performance, it seems conservatism cannot be observed. Predetermined amortisation appears to be an expedient alternative, providing the gap between these two approaches is not too big. This approach is easy and cheap to apply, and it tends to give a smoother earnings performance, which might be welcomed by managers. Nevertheless, if the gap between these two approaches is too big, then amortisation charges are arbitrary and meaningless. Taking all these into consideration, it is likely to suggest that a predetermined amortisation approach together with periodical impairment testing may have the potential to best present the diminution in the value of goodwill. My results from the contributions of goodwill acquired over past years are inconclusive as to whether goodwill depreciates or how it depreciates. Under such circumstances, it is perhaps best to review its values at specified intervals to make sure its value is maintained or, if the value is impaired, decide the appropriate amortisation charges. Arbitrary amortisation cannot faithfully represent the decrease in its value in this respect. However, considering the inherent technical difficulties and the possibility of going against conservatism in impairment testing, the study is inclined to suggest the best practice perhaps is the predetermined amortisation supplemented with periodical impairment testing, as it takes account of the accounting qualities – relevance and reliability as well as conservatism.

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