

GOODWILL IMPAIRMENT: THE CASE OF HONG KONG

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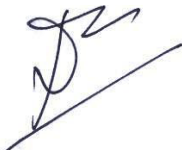
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CERTIFICATION

This thesis is submitted in fulfilment of the degree of PhD at Macquarie Graduate School of Management, Macquarie University. It is wholly my own work, except when general and specific references are acknowledged. I hereby certify that this document has not been submitted for a higher degree to any other university or institution.

Signed

A handwritten signature in blue ink, appearing to be 'Dung Manh Tran', with a long horizontal stroke extending to the right.

Dung Manh Tran

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ABSTRACT

This thesis focuses on goodwill impairment implemented and practised in the first three years after Hong Kong's adoption of the International Financial Reporting Standards (IFRS). Three issues – compliance, discount rate and audit quality with respect to goodwill impairment testing – are the focus of analytical and empirical attention.

Understandably, one of the most controversial issues that has been discussed in financial reporting is goodwill. Goodwill impairment is argued to be one of the most difficult issues in practice. This thesis commences with a review of literature relating to goodwill with regard to its conceptualisation, techniques to avoid or alter its recognition, ways to measure and adjust it, and a description of key technical requirements of goodwill impairment in the context of Hong Kong. These issues are demonstrably reviewed in this thesis.

This study focuses on filling the gap in knowledge of compliance, discount rate and audit quality in relation to goodwill impairment. To do so, detailed annual reports of listed firms collected from the Main Board of the Hong Kong Stock Exchange in the period from 2005 to 2007, were drawn upon. Employing analytical procedures and the Capital Asset Pricing Model (CAPM), the study provides persuasive evidence on the issues of compliance, discount rate and audit quality with respect to goodwill impairment.

The thesis concludes that the rates of non-compliance and poor quality of disclosure pertaining to goodwill impairment conducted by Hong Kong firms reduced in the first three years after Hong Kong's adoption of IFRS. However, non-compliance levels and poor disclosure quality were still high. The sample firms had a tendency to

understate discount rates in comparison with independently estimated discount rates in all three years of the investigation. In addition, audit quality among the Big 4 auditors is proved to be heterogeneous rather than homogeneous.

The thesis concludes that a big gap exists between the standard requirements of goodwill impairment and practice. In the context of Hong Kong, this research demonstrates that the efficacy of this standard is low. It is therefore likely that the application of goodwill impairment in practice will continue to cause concern for policy makers and standard setters.