

Study on Accounting Motivation of Goodwill Impairment Treatment—Taking Tianshen Entertainment Co., Ltd., as an example

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Abstract. Merger and acquisition can help companies develop better and faster, but it will also create a risk of goodwill impairment for the high goodwill generated during the process. In this paper, Tianshen Entertainment Co., Ltd. was taken as an example to analyze the formation of its goodwill as well as the goodwill impairment, and discussed the motivation of its huge goodwill impairment from different perspectives. The results show that: Tianshen Entertainment Co., Ltd. had a great motivation to manipulate its financial situation due to the poor macroeconomic and industry environment in 2018, as well as the high goodwill of its company. So this paper would put forward relevant suggestions on goodwill impairment from multiple perspectives based on such phenomenon.

1. Introduction

Nearly 300 of the more than 2,500 listed companies took goodwill as a reason for performance change in their 2018 performance forecast as of mid-February 2019. For example, Chongqing Fuan Pharmaceutical (Group)Co., Ltd. planned to have goodwill impairment of 610 million yuan and Tianshen Entertainment Co., Ltd. planned to have goodwill impairment of 4.814 billion yuan. The massive goodwill impairment of listed companies damaged the confidence of investors and disturbed the order of the capital market seriously. Moreover, it would bring a huge impact on the capital market and form a systemic financial risk if many listed companies impaired their goodwill at the same time [1]. Goodwill has long been one of the most important issues in the capital market, and the potential risk of goodwill impairment cannot be underestimated [2]. Therefore, this paper took Tianshen Entertainment Co., Ltd. the king of loss in 2018, as an example, used case analysis to analyze the motivation of goodwill impairment of Tianshen Entertainment Co., Ltd. from multiple perspectives and put forward corresponding suggestions.

2. Literature review

2.1 Goodwill

As the expected future excess returns and the discounted value of capacity, goodwill should be recognized as an asset in the financial statements. Goodwill refers to the difference between the purchase price and fair value of an enterprise's net assets [3]. The essence of goodwill is a kind of synergistic effect [4]. And goodwill is the ability to obtain excess returns in the future of assets acquired by merger and acquisition essentially. Goodwill cannot become the "emperor's new clothes" that damages the interests of investors [5]. The economic nature of goodwill can be summarized as: "the persistence of goodwill", "goodwill must have the possibility of transfer" and "goodwill can be measured in currency" [6]. The various unaccounted advantages and factors that enable the company to obtain excess returns can be included in the goodwill account. Based on the research of others, Sheldon Horowitz put forward the "ternary theory" which is the good value theory, excess value theory and total price account theory [7].

2.2 Impairment of goodwill

The proportion of goodwill impairment provision is significantly different between profitable and loss companies. Losing listed companies are more inclined to accrue more goodwill impairment provisions. Management took goodwill impairment as a mean to adjust profits [8]. From the perspective of performance commitment, the performance commitment of the target company played an obvious supporting role in merger and acquisition with high valuation premium [9]. After the disclosure of goodwill impairment information, the profitability of the listed company will decline, and investors will reduce their expectations of the company's future profitability due to goodwill impairment. In order to bring benefits by being acquired by listed companies, some small and medium-sized companies exaggerated their performance to obtain high performance and high valuation, and the acquirer accepted such high premium merger and acquisition in the case of information asymmetry [10].

3. The theory of motive of accounting treatment of impairment of business goodwill

Generally speaking, the accounting motivation of goodwill impairment can be divided into three levels: macro, medium and micro.

3.1 Macroeconomic environment

Since the macroeconomic environment is the background of the development of companies, the performance of companies is closely related to the macroeconomic environment. When the macroeconomic environment is in poor operation, the company considers the goodwill impairment or even impair a huge amount of their goodwill in order to take the opportunity to “big bath” of the financial situation of the enterprise.

3.2 Medium environment

The medium environment refers to the industry environment. There will be differences in the various financial indicators between different industries, and the influence of industry factors on business is showed in the formation of goodwill and the subsequent measurement period of goodwill. In the formative period of goodwill, the goodwill level of industries such as media industry and computer industry is higher than that of other industries, which is mainly due to the high dependence of emerging industries on outward acquisition, resulting in extremely high goodwill accumulation. In the subsequent measurement stage of goodwill, although there are different methods of impairment testing, the assets of the enterprise are tested on the basis of the industry environment.

3.3 Microeconomic environment

The operating conditions of companies can usually be manipulated through false profits and profit smoothing. Companies use profit smoothing to avoid excessive fluctuations in corporate profitability. In addition, companies will use "reasonable" accounting treatment to manipulate their financial situation when they are facing with risks such as delisting and special treatment. Therefore, a company can adjust its profit and loss by manipulating the impairment of goodwill, but this will also increase the investment risk of investors and harm their interests.

4. Case study

4.1 Company introduction

Formerly known as Beijing Tianshen Interactive Technology Co., Ltd., Tianshen Entertainment Co., Ltd. was founded in 2010 by major shareholder Zhu Xi and others. It changed its name to Dalian Tianshen Entertainment Co., Ltd. (Tianshen Entertainment Co., Ltd. for short) after successfully listed on the Shenzhen Stock Exchange through a backdoor acquisition. Tianshen Entertainment Co.,

Ltd. is an internet company that main business includes mobile game and web game development, mobile internet platform service and film and television entertainment business.

This paper selected Tianshen Entertainment Co., Ltd. based on the following two principles: representation and enlightenment. On one hand, relied on the capital operation, Tianshen Entertainment Co., Ltd.'s revenue increased by 5.52 times and the net profit attributable to the parent company increased by 31.02 times to 1.016 billion yuan from 2014-2017. However, it became the "king of loss" in 2018, and the loss of net profit was about 7.3 billion yuan which included 4.1 billion yuan of goodwill impairment. It was no coincidence that Tianshen Entertainment Co., Ltd. suffered from the goodwill impairment due to its enormous goodwill while many listed companies also stepped on the "mines" in 2018. The reasons for such great change are the actions taken by it, for instance, large-scale combination, continuous acquisitions of high-growth companies, etc., are the epitome of the market. Therefore, the goodwill impairment of Tianshen Entertainment Co., Ltd. is extremely representative. On the other hand, the decision-makers of Tianshen Entertainment Co., Ltd. hid the high goodwill impairment risk by using the loopholes of long goodwill longevity to buy "performance" in a high price, and this was not only a way for Tianshen Entertainment Co., Ltd. to manipulate the financial reports but also a common method used by the listed companies. Therefore, the analysis of Tianshen Entertainment Co., Ltd. helped to propose a more complete prevention method for the risk of goodwill impairment caused by acquisitions as well as to solve the shortcomings of goodwill treatment, which is instructive for future goodwill treatment.

4.2 Case analysis

4.2.1 The goodwill of Tianshen Entertainment Co., Ltd.

According to the 2018 annual report of Tianshen Entertainment Co., Ltd., it consists of 75 subsidiaries which include 44 for software and information technology services, 11 for advertising and mobile Internet advertising, 8 for investment management and 12 for other use. Besides, 51 subsidiaries are acquired by the combination of non-identical control. Tianshen Entertainment Co., Ltd. formed its goodwill of up to 6.7 billion through multiple premium acquisitions during 2015-2018, this was shown in Table 1. Through the acquisition of Beijing Miaoquhengsheng Network Technology Co., Ltd., Shenzhen Weiaipu Information Technology Co., Ltd., Leishang (Beijing) Technology Co., Ltd. and Avazu and Shanghai Maicheng Network Technology Co., Ltd. in 2015, the annual goodwill of Tianshen Entertainment Co., Ltd. was 3.664 billion yuan, accounting for 50.16% of the total assets. After the acquisition of Shenzhen YiHua Technology Co., Ltd. in 2016, the accumulated goodwill of Tianshen Entertainment Co., Ltd. reached 4.566 billion yuan, accounting for 61.61% of total assets. And Tianshen Entertainment Co., Ltd. didn't stop acquiring in 2017, on the contrary, it acquired Beijing Huanxiagyueyou Network Technology Co., Ltd., Beijing HerunDetang Culture&Media Co.,Ltd, Jiaxing Lewan Network Technology Co., Ltd. and Beijing Xingkongzhisheng Technology Development Co., Ltd. during the year, which caused the accumulated goodwill reached to 6.571 billion, accounting for 46% of total assets. In 2018, the accumulated goodwill was 6.708 billion yuan, accounting for about 78% of the total assets. The value of Tianshen Entertainment Co., Ltd.'s goodwill has almost half of the total assets in the past four years, which makes Tianshen's business performance and profitability very impressive, but in the face of such high goodwill, Tianshen Entertainment Co., Ltd. will either reduce it through one-time impairment or year by year review. However, no matter which method is adopted to impair the goodwill, the interests of small and medium investors will be damaged and bring investment risks to investors.

Table 1 The goodwill of Tianshen Entertainment Co., Ltd. from 2015 to 2018

Acquired Company	Year	Total condition	Million yuan	
			Net identified assets at acquisition date	Goodwill
Beijing Miaoquhengsheng Network Technology Co., Ltd.	2015	620	107	513
Shenzhen Weiaipu Information Technology Co., Ltd.	2015	600	116	484
Leishang (Beijing) Technology Co., Ltd.	2015	880	97	783
Avazu and Shanghai Maicheng Network Technology Co., Ltd.	2015	2,080	1,948	132
Shenzhen YiHua Technology Co., Ltd.	2016	986	84	902
Beijing Huanxiagyueyou Network Technology Co., Ltd.	2017	3,417	222	3,195
Beijing HerunDetang Culture&Media Co., Ltd.	2017	742	489	253
Jiaxing Lewan Network Technology Co., Ltd.	2017	469	33	436
Beijing Xingkongzhisheng Technology Development Co., Ltd.	2017	94,274	31,280	62,994

Note: Based on the annual report of Tianshen Entertainment Co., Ltd. from 2015 to 2018

4.2.2 The goodwill impairment of Tianshen Entertainment Co., Ltd.

Due to the unfulfilled commitments of Avazu and Shanghai Maicheng Network Technology Co., Ltd. in 2016, the goodwill impairment of Tianshen Entertainment Co., Ltd. was 13.6496 million yuan after assessing by Beijing Guorongxinghua Assets Appraisal Co.,Ltd. In 2017, Tianshen Entertainment Co., Ltd. transferred its corresponding goodwill by reducing its shares in Avazu, which caused goodwill impairment in Avazu as well as Miaoquhengsheng of 30.38 million yuan after assessing by Beijing North Asia Asset Assessment Firm. And another goodwill impairment of 4.9 billion yuan after assessing by Beijing Zhuoxindahua Assets Appraisal in 2018. It was all shown in Table 2. From 2015 to 2017, the goodwill impairment accounted for less than 1% of the book value of goodwill but 60.97% in 2018, so it is reasonable to suspect that Tianshen Entertainment Co., Ltd. was using the goodwill impairment to take a big bath since the amount was extremely enormous.

Table 2 The goodwill impairment of Tianshen Entertainment Co., Ltd. from 2015 to 2018

Year	Million yuan			
	2015	2016	2017	2018
Goodwill impairment	0	14	30	4,090
Book value of goodwill	3,664	4,566	6,572	6,708
Goodwill impairment/Book value of goodwill	0%	0.30%	0.46%	60.97%

Note: Based on the annual report of Tianshen Entertainment Co., Ltd. from 2015 to 2018

4.2.3 Analysis of the motivation of goodwill impairment of Tianshen Entertainment Co., Ltd.

Although different treatment of reversal asset is used between Chinese accounting standards and International accounting standards, they are consistent with the goodwill impairment-using the impairment test method to review the goodwill annually and should not be reversed once it has been impaired. However, since goodwill is intangible, unrecognizable and does not generate cash flow independently, the judgment of goodwill impairment will greatly depend on the professional level of accountant, which provides space for companies to use goodwill impairment for financial manipulation. This paper would analyze the motivation of Tianshen Entertainment Co., Ltd.'s goodwill impairment from the macro, medium and micro levels based on the above research.

The micro level. The goodwill and goodwill impairment of listed companies in China have increased year by year from 2014 to 2018, and the goodwill of listed companies has reached 1,307.6 billion yuan together with goodwill impairment 165.9 billion yuan in 2018. It can be seen that the market's goodwill bubble had already formed and how to eliminate such high goodwill has become a difficult problem for listed companies. Besides, the A-share market in 2018 was in full swing throughout the year and its performance was not satisfactory due to the impact of China-US trade war and deleveraging. The Shanghai Composite Index fell 23.31%, Compositional Index of

Shenzhen Stock Market fell 42.73% and the Growth Enterprise Market fell 27.07% as of December 20, 2018, which provided an opportunity for companies to impair their goodwill. At the beginning of 2019, listed companies disclosed changes in performance forecast. Among the 332 companies with the first loss, 149 companies were affected by the impairment of goodwill. Many companies took advantage of the bear market to have "big bath", and Tianshen Entertainment Co., Ltd. became the king of loss in 2018 for losing 7.3- 7.9 billion yuan.

The medium level. Due to the characteristics of the media and entertainment industry, it is easier to generate higher goodwill than other industries. The media industry is the top industry among the top ten industries with a drop of more than 30% in the stock market with a total retreat of 37.89% in 2018. After Cui Yongyuan disclosed the scandal in the entertainment on Weibo on May 28, 2018, the media sector evaporated the market value of over 10 billion overnight. Although the main business of Tianshen Entertainment Co., Ltd.'s parent company is the Internet game, its subsidiaries operate in the entertainment and film industry, which has a certain impact on the company's annual operating results. Therefore, Tianshen Entertainment Co., Ltd. may take this opportunity to manipulate goodwill impairment to reduce the pressure of company's high goodwill.

The micro level. The total asset turnover rate of Tianshen Entertainment Co., Ltd. in 2011-2018 was 0.54, 0.41, 0.43, 0.55, 0.23, 0.23, 0.28, 0.23, indicating that its asset operating efficiency had decreased and various assets had not been used effectively after a series of mergers and acquisitions. In addition, the net profit of Tianshen Entertainment Co., Ltd. was generally on the rise and performed well during 2011-2017, but it suddenly made a huge loss of 7.3-7.9 billion in 2018. Therefore, it is possible for Tianshen Entertainment Co., Ltd. to use goodwill impairment to avoid being special treated in the subsequent year.

5. Conclusion

This paper used the case analysis method to study the motives of Tianshen Entertainment Co., Ltd.'s goodwill impairment in 2018 from the macro, medium and micro perspectives. The results showed that: the company is likely to use one-time goodwill impairment to reduce the level of companies' high goodwill when the overall economic environment is poor. Therefore, the following suggestions are made: 1) Improve the company's internal audit. The internal audit department should exist as an independent department in the company and audit the problems independently. 2) Improve the audit quality of accounting firms. Not only should the accounting firms select the clients carefully and make professional judgments on the problems of the audited company, but also avoid the conflicts of interest during the audit to ensure the success of the audit. 3) The regulatory authorities should improve the standard of goodwill impairment. After the change of accounting standards in 2006, the criteria for goodwill impairment are more in line with its essence, but still provide space for accounting manipulation. Therefore, the accounting standards should be revised constantly according to the actual situation to reduce the space for companies to manipulate financial reports.

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