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Market Reaction to Goodwill Impairments

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Abstract

This paper examines the information content of goodwill write-downs under International Accounting Standard (IAS) 36 (Impairment of Assets) and Statement of Financial Accounting Standards (SFAS) No. 142. We investigate whether the informational value depends on the reliability of the news. Using a sample of 564 goodwill write-down announcements issued from 2005 to 2009, we find a negative capital market reaction to announcements of unexpected goodwill write-offs. Our results indicate that investors react more negatively when a country's level of legal protection is low.

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Notes


1 Throughout the paper, we refer to partial and complete downward goodwill revaluations with the term write-down.

2 An important caveat of this study, therefore, is that a goodwill impairment announcement must have been available. If a firm did not release such information or if the press release was not included in the database or identified during our search, it is not included in our sample.

3 Our study focuses on unexpected write-offs where the announced impairment amount exceeds the write-off expected by investors. Our study contains no predictions for situations where the announced impairment amount is below the expected amount.

4 We thank an anonymous reviewer for this line of inquiry.

5 Prior to the introduction of SFAS 142, US GAAP also allowed firms that met certain criteria to account for business combinations by using the pooling of interest method. Under this method, firms did not have to amortize purchased goodwill, so that the



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level of disclosure does not imply less management discretion when computing the goodwill write-off.

16 We acknowledge that IFRS are applied in many other countries around the world. In our study, we focus on their application in Europe, since they have a long tradition as accounting standards in the European Union.

Additional information

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