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The Proposal and Application of the Research Framework of Enterprise M&A Goodwill Risk—Taking the Media Industry as an Example

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Abstract. In the past ten years, the mergers and acquisitions of Chinese enterprises have entered a period of high tide. The high valuation and high-value mergers and acquisitions have produced huge goodwill. The goodwill faces potential impairment risks, which has a very negative impact on the company's future performance. However, most listed companies currently prefer not to accrue or reduce the impairment of goodwill. At the same time, due to the inherent light asset characteristics of the media industry, the risk of income is high, and the issue of goodwill is particularly prominent. Therefore, this paper attempts to analyze the existence of goodwill risk points from the case of the media industry merger and acquisition failure, the case of Guangdong Media's acquisition of Xianglili Media. From the perspective of solving practical problems, the research framework of goodwill risk in enterprise mergers and acquisitions is proposed, and the process framework of forecasting and identifying, evaluating and analyzing, controlling and coping with the goodwill risk in the capital market is rationally designed. The research results show that this analysis framework is applicable to most enterprises, and it has strong operability. It is of great significance to deal with the prevention and prevention of goodwill impairment risk. It is hoped that in the future, the risk of goodwill will attract more attention, and enterprises can better avoid the risk of goodwill and make the capital market develop healthily.

Introduction

Research Background

From the perspective of the development of the times, all countries in the world are developing rapidly. The process of world economic integration has also promoted the development and growth of enterprises in all countries. According to the statistics of Qingke Research Center, from 2008 to 2015, the total number of mergers and acquisitions in China reached 9,098, and the amount of mergers and acquisitions increased year by year, from 236.595 billion US dollars in 2008 to 104.375 billion US dollars in 2015, with a total growth rate of 26.92%. This shows the hot trend of mergers and acquisitions. What needs to be vigilant is that a large number of mergers and acquisitions will lead to concentrated risks of mergers and acquisitions bubble.

Huge amount of goodwill will inevitably bring uncontrollable impairment risk of goodwill. According to the current accounting standards in China, once goodwill is confirmed, it cannot be reversed. Therefore, the impairment loss of goodwill will directly affect the net profit amount in the consolidated statement, devour the overall value of the enterprise, and cause irreparable negative impact on the performance of the enterprise.

Research Significance

In the current situation of accounting research, there are fewer prevention issues related to the impairment risk of goodwill, so that there is no unified conclusion. By combing the essence of goodwill, this paper gives a theoretical overview of the goodwill of mergers and acquisitions, which is conducive to sorting out the outline of the risk of goodwill impairment, helping to analyze the theoretical research in relevant fields, and in-depth research on the method of measuring and depreciating the goodwill of mergers and acquisitions. . For the business operators, they can also better understand the goodwill and accurately estimate the relevant assets in the asset evaluation, which can also make the success rate of the company in the M&A activities higher.

Introduction of Relevant Theories

Definition of Goodwill

Among the accounting scholars in China, Yang Rumei (1926) explained goodwill earlier: "Anyone who can make an enterprise produce a kind of common high income can be called goodwill." According to China's existing accounting standards, goodwill is defined as goodwill: in the merger of enterprises under different control, the merger cost of the purchaser is greater than the fair value of the purchased party's identifiable net assets, which should be recognized as goodwill. International Accounting Standards (IAS) defines goodwill as that the merger cost paid by the buyer is greater than its share in the fair value of the identifiable net assets owned by the seller.

To sum up, up to now, there are many studies on the definition and nature of goodwill at home and abroad, but no consensus has been reached in both theoretical and practical circles. The most widely accepted theory of excess return is synthesized.

Definition of Consolidated Goodwill

Consolidated goodwill, also known as purchased goodwill, refers to the difference between the amount of merger and acquisition granted by the merged enterprise and the sum of the fair values of the identifiable net assets of the merged enterprise in the process of merger and reorganization. This is also the definition of China's new accounting standards for enterprises in 2014, and is also the view of financial accounting standards board (FASB). The formula is as follows:

Consolidated Goodwill = Investment Cost-Fair Value of Net Assets. (1)

In accounting academia, there is no standard and conclusion for the definition of goodwill, but there is a general definition of merged goodwill: goodwill can be recognized as merged goodwill in merger and acquisition according to the purchase cost method.

Impairment of Goodwill

Impairment of goodwill refers to the corresponding impairment loss confirmed after the impairment test of the formed consolidated goodwill in the process of merger and acquisition of enterprises. According to the standard "Accounting Standards for Enterprises No.8-Impairment of Assets" formulated by the Ministry of Finance of China, "consolidated goodwill shall be tested for impairment at least once at the end of each fiscal year in combination with its related asset group or combination of asset groups". This standard was promulgated and implemented in 2007, which puts forward higher requirements for the order of the capital market and gives accounting practitioners in enterprises greater policy choice.

Goodwill Impairment Risk

Goodwill impairment risk refers to the possibility of goodwill impairment loss in the goodwill impairment test. The possibility of negative impact is goodwill impairment risk, which will bring negative consequences to the financial statements of enterprises. According to the current accounting standards, once an enterprise recognizes the impairment of goodwill, it must be included in the profits and losses of the current period, which will affect the profit level of the enterprise in the current period, adversely affect the image of the enterprise and have a negative effect on the stock price of the listed company. Enterprises will be greatly impacted when facing the risk of goodwill impairment, and will be more or less affected by the risk. Therefore, it is necessary and important to prevent the risk of goodwill impairment.

Proposal and Application of Goodwill Risk Research Framework for Mergers and Acquisitions of Enterprises-Taking Media Industry as an Example

As one of China's important strategic pillar industries, cultural media industry is one of the indispensable links in China's economic and social development.

The media industry has the characteristics of light assets and unstable products. There is no exact historical data for reference when predicting revenue. The subjectivity of prediction is strong, which makes it difficult to calculate its revenue and the risk of revenue is high. Therefore, it is the industry with the greatest goodwill risk among all industries and has high attention and profit space. Therefore, this industry is the starting point to explore the goodwill risk.

Research on Typical Cases of Media Industry-Guangdong Media Merger and Acquisition of Champs Elysees Media

Case Introduction.

(1) Merger and Acquisition Party: Guangdong Media

Guangdong Guangzhou Daily Media Co., Ltd., established in 1992, is a listed company controlled by Guangzhou Daily Newspaper Group, also known as Guangdong Media. It belongs to the scope of newspaper industry and printing industry in the media industry. The company was listed on Shenzhen Stock Exchange in 2007 with stock code 002181, ranking fifth in the growth capacity in the media industry, and has great development potential in the next few years. From 1994 to 2013, the advertising revenue of Guangdong media has been ranked first in the national newspaper industry.

(2) Acquired party: Champs Elysees Media

Shanghai Champs Elysees Media Co., Ltd. was established in 2003. Since entering the outdoor LED large screen advertising market in 2006, it has become the leader of large outdoor LED media in China. Outdoor LED screens have a large market share and have considerable advantages.

(3) M&A process

In July 2014, in order to enter the field of outdoor LED large-screen media, Guangdong Media, after a resolution, bought a 100% stake in Shanghai Champs Elysees Advertising Media Co., Ltd. for a consideration of 450 million yuan, and signed the document "Profit Forecast Compensation Agreement". However, in 2015, Champs Elysees suffered a huge loss of 374 million yuan. The company's financial situation was poor and it was insolvent, causing its acquisition company Guangdong Media to be mired in debt.

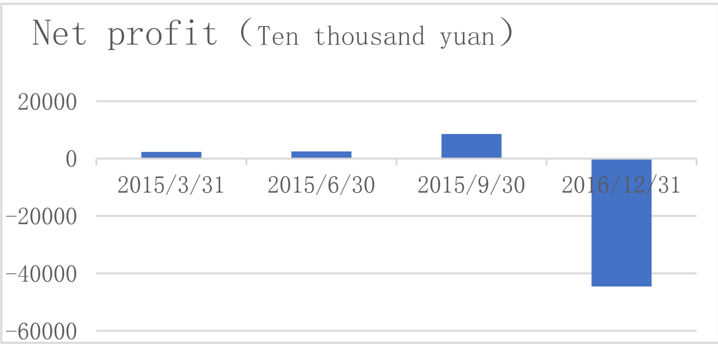

Fig.1 Bar chart of Guangdong media's net profit in 2015

As shown in the above figure, Guangdong Media has seen a sharp drop in net profit at the end of 2015 after its wholly-owned acquisition of Champs Elysees in 2014.In the first and second quarters of 15 years, the net profit in September was 85.685 million yuan, but at the end of the third quarter, the net profit dropped to 44.542 million yuan. In the same year, General Manager Ye Mei of Champs Elysees was arrested and investigated by Guangzhou police on suspicion of contract fraud. On September 10, 2016, Guangdong Media announced the bankruptcy liquidation of its subsidiary Champs Elysees.

Case Analysis.

(1) First, Guangdong Media's Risk Forecast and Identification of Goodwill in Capital Market Mergers and Acquisitions.

Guangdong Media failed to accurately identify the goodwill risk in the merger and acquisition, paid less attention to goodwill, and failed to select the merger and acquisition object. It stipulates that Champs Elysees will have to compensate 18 million yuan of stock agency fees if it cannot be listed before May 31, 2014.At the same time, Champs Elysees also concealed more than 13 million yuan owed to the bank. As a result, serious information asymmetry occurred and the first identification step of goodwill risk failed.

	A	B	C	D	E	F	G
1	Index name	2018/12/31	2017/12/31	2016/12/31	2015/12/31	2014/12/31	2013/12/31
2	Basic Earnings Per Share (RMB)	0. 047	0. 0625	0. 1632	-0. 3836	0. 3253	0. 4451
3	Deduction of non-earnings per share (RMB)	-0. 168	0. 0807	-0. 138	-0. 3741	0. 3083	0. 4508
4	Diluted earnings per share (yuan)	0. 047	0. 0625	0. 1632	-0. 3836	0. 3253	0. 4451
5	Net Income Attribution (RMB)	5454. 07 (ten thousand)	7255. 12 (ten thousand)	1. 90 (Billion)	-5391. 00 (ten thousand)	2. 30 (Billion)	3. 08 (Billion)
6	Net attributable profit increased year-on-year (%)	-24. 82	-61. 72	--	-293. 96	-25. 44	11. 72
7	Rolling annular growth of attributable net profit (%)	-64. 8	-72. 66	--	-333. 41	14. 64	9. 75
8	Weighted return on net assets (%)	1. 38	1. 88	5. 14	-10. 83	5. 62	8. 29
9	Rate of return on diluted net assets (%)	1. 38	1. 85	5. 01	-12. 4	5. 28	8. 02
10	Gross profit margin (%)	30. 54	28. 54	24. 86	29. 47	41. 94	40. 16
11	Actual tax rate (%)	1	17. 26	-0. 73	--	7. 78	-0. 5
12	Advance/Operating Income	0. 19	0. 17	0. 15	0. 13	0. 14	0. 13
13	Sales Cash Flow/Operating Income	1. 11	1. 11	1. 03	1. 05	0. 97	1. 08
14	Total asset turnover rate (sub)	0. 18	0. 2	0. 23	0. 27	0. 35	0. 4
15	Asset-liability ratio (%)	9. 77	8. 72	19. 03	17. 5	13. 91	10. 32
16	Current liabilities/total liabilities (%)	96. 79	95. 07	94. 21	95. 63	95. 17	98. 25

Fig.2 Major financial data of Guangdong media from 2012 to 2017

(2) Second, the risk assessment and analysis of the goodwill of Guangdong media in the capital market.

It can be seen that its main financial data basically showed a sharp downward trend in the second year of merger and acquisition, that is, at the end of 2015, Guangdong Media's basic earnings per share fell from 0.45 yuan/share in the previous two years to -0.38 yuan/share, a decrease of 218.75%. The figure was 311.46 million yuan at the end of the 2013 accounting period, and the operating profit dropped sharply to-435.71 million yuan in 2015. From the ultra-low profit of the enterprise this year, it can be seen that the merger has a great impact on the main business of the enterprise.

(3) Third, Guangdong Media's Risk Control and Response to Goodwill in Capital Market Mergers and Acquisitions.

Before the formal M&A, Guangdong Media signed a gambling treaty with Champs Elysees on "Profit Forecast Compensation Agreement" in order to reduce the goodwill risk of M&A. According to the agreement of both parties at that time, more than 20 people including general manager Ye Mei and others at the middle and senior level of Champs Elysees promised Guangdong Media that the net profit after tax of Champs Elysees Media should be no less than 56.83 million yuan, 68.7 million yuan and 81.56 million yuan respectively in 14 years, 15 years and 16 years. Analysis of its historical data shows that the net profit of Champs Elysees Media in 2011 was 36.47 million yuan, with the total income of that year approaching 200 million yuan.Net profit in 2012 was 36.95 million yuan. In 2016, Champs also declared bankruptcy due to a total debt of 339 million yuan, which was much higher than the total assets. It finally declared that the case of Guangdong Media’s acquisition of Champs Elysees failed completely.

Case Resolution-Research Framework for Goodwill Risk in Mergers and Acquisitions

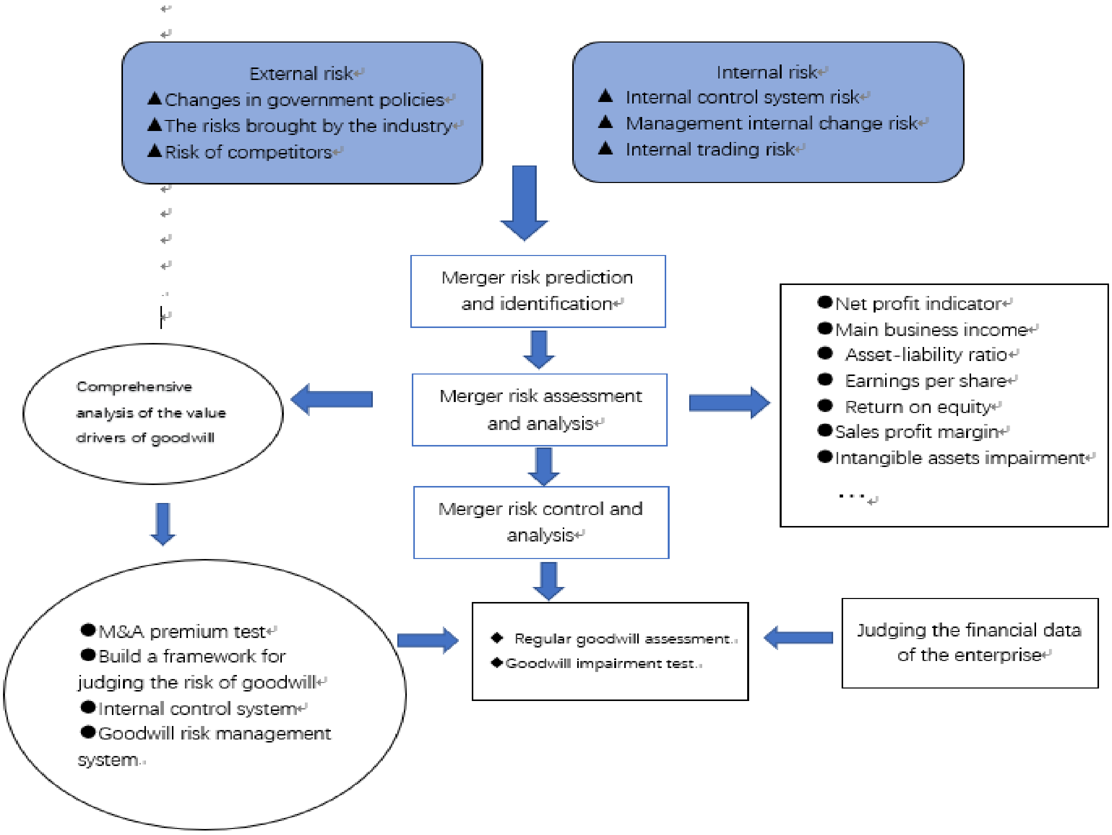

Fig. 3 Corporate M&A goodwill risk research framework

Capital Market M&A Goodwill Risk Prediction and Identification.

In the complicated capital market, enterprises should pay special attention to the changes in the surrounding economic situation. Therefore, it is necessary and important to predict and identify the goodwill risk in the process of merger and acquisition, which should be taken as the starting point for goodwill risk analysis.

Identification of External Potential Risks

Changes in government policies. Changes in government policies often indicate the trend and trend of an industry or even the entire economy.

Risks brought by the industry. The enterprise develops in the industry, so we should pay close attention to the current situation and development trend of the industry in which the enterprise is located, pay attention to which sub-sectors the high profit rate of the industry appears, and then adjust our strategic layout.

Identification of Internal Potential Risks

Risks brought by internal control system. The internal control system of an enterprise is an important criterion for whether it has an efficient management level. If there are many risks in the internal control of an enterprise, its contingent risks will increase and hidden information will easily affect the judgment. In this case, goodwill risks will also be greater.

Capital Market Merger Goodwill Risk Assessment and Analysis.

From the point of view of capital market, to judge the goodwill risk of an enterprise, it is necessary to analyze the influence of various evaluation indexes on the financial data of the enterprise, analyze the net profit index, main business income and liabilities before and after the merger and acquisition of the enterprise, and obtain the influence degree of the existence of the risk on the enterprise. This part of the content can clearly observe its data changes through specific case descriptions.

Capital Market Merger Goodwill Risk Control and Response.

First of all, to control the risk of goodwill requires the company from shareholders, management to managers and employees to pay attention to the value of goodwill from the concept, understand the harm that goodwill risk may bring, carefully study the links that may cause problems in the company, and carry out corresponding control and prevention. Secondly, the evaluation framework of goodwill risk should be constructed on the basis of the emphasis on concept, which requires a special task team to study and formulate a goodwill risk management system. Finally, goodwill needs to be regularly evaluated and tested for impairment, so as to find out the value level of goodwill in different stages according to the changes of the enterprise in time, so as to grasp the risk level of goodwill in time.

Research Conclusions

China's media industry is actually in a rising and expanding stage and needs to explore the law and develop in an exploratory way. Although Guangdong Media Company has strong strength, it is unavoidable to make mistakes in the industry's M&A boom and lose profits in the high-risk field of goodwill. Therefore, it has great reference significance and enlightenment for other enterprises in the media industry.

Listed companies in the capital market generally do not pay enough attention to goodwill and have not formed a management framework for goodwill risks. In order to reduce the negative impact of goodwill risk, the goodwill risk of capital market mergers and acquisitions should be managed according to the order of capital market mergers and acquisitions goodwill risk prediction and identification, capital market mergers and acquisitions goodwill risk assessment and analysis, capital market mergers and acquisitions goodwill risk control and response.

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