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Staff paper

Agenda reference: 3

Accounting Standards Advisory Forum

Date	**July 2023**
Project	**Business Combinations—Disclosures, Goodwill and Impairment**
Topic	**Improving disclosures about business combinations**
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Agenda

Purpose of the meeting

The staff will present an education session on the IASB's proposals to require an entity to disclose better information about business combinations. In particular, the staff will discuss what information the IASB's proposals are intended to capture and how the proposals are intended to work.

Background

Background

Objective

To improve the information entities provide to users of financial statements (users), at a reasonable cost, about the business combinations those entities make.

Path forward

The IASB redeliberated its preliminary views in the Discussion Paper, taking into account stakeholders' feedback on those preliminary views. The IASB will publish an exposure draft with revised proposals.

Project History

2013–2015	March 2020	March 2021—Present	H1 2024
PIR of IFRS 3	Discussion Paper	Project redeliberation	Exposure draft

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The IASB’s tentative decisions

	Tentative decisions made by the IASB	What has changed from IASB’s preliminary views
Disclosures about business combinations	• Disclose subsequent performance information of **strategically important business combinations** • **Exempt an entity from disclosing some information in specific circumstances** • Other improvements to existing disclosures, including quantitative information about expected synergies	• Disclosure is required for a more targeted subset of business combinations • Entities are now exempted from disclosing some information in specific circumstances • Management is defined as an entity’s key management personnel (KMP) instead of chief operating decision maker (CODM)
The accounting for goodwill	• Retain the impairment-only model for the subsequent accounting of goodwill • Retain requirement to perform impairment test annually • Simplify calculation of value in use	• Retaining the annual quantitative impairment test • The IASB is exploring ways to improve the effectiveness of the impairment test

A balanced package of proposals

Overall package	
	• **Balance between providing useful information while keeping costs at a reasonable level** • **Help users more effectively assess management's decision to acquire a business**

	Improve information at a reasonable cost	Reduce cost and complexity without reducing information
Disclose performance of business combinations	✓	
Improve existing disclosures (expected synergies, pro forma etc)	✓	
Improve impairment test effectiveness	The IASB will discuss possible improvements in July 2023	
Simplify value in use		✓

Improving disclosures about business combinations

Overall Feedback

Overall message	Many respondents, including almost all users, agreed with the preliminary views. However, many respondents, including almost all preparers, disagreed. Respondents identified costs associated with the preliminary views

Summary of feedback

- Most preparers disagreed with the preliminary views because they expect the **costs of the disclosures to outweigh the benefits:**
  - **Monetary costs:** for example, costs of collecting and auditing the information; and
  - **Proprietary costs:** for example, from disclosing information some consider to be commercially sensitive and potential litigation
- Many respondents said information about the performance of business combinations should be provided in **management commentary rather than financial statements**

Feedback

The management approach	Costs

Feedback summary:
• Most agreed the use of a management approach would help reduce cost of compliance. However, some said that the reduction in the costs is not sufficient
Is the CODM the right level of management?
• Mixed feedback:
  • many said using CODM to identify business combinations is a practical approach
  • many said using CODM may result in users not receiving all material information or too much information
  • we observed confusion about the link between the preliminary views and segment reporting
	4 key contributors to cost:
	• **Commercial sensitivity**—disclosure could contain sensitive information that, if disclosed, could harm the entity
	• **Forward-looking**—disclosure could contain information about the future that, if disclosed, could increase litigation risk
	• **Integration**—entity might not be able to disclose information that is representative of the performance of a business combination if the acquired business is integrated into the entity’s existing operations
	• **Auditability**—some information that would be required by the preliminary views might be costly, or difficult, to audit

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IASB’s response

Feedback	IASB’s response
• Information belongs in management commentary	• Reconfirmed its preliminary view that the information can be required in financial statements (slide 12)
• Information could be commercially sensitive or forward-looking	• Exempt an entity from disclosing some information in specific circumstances (slide 13)
• Entities might be required to disclose too much information	• Require disclosure of information for only strategically important business combinations (slide 14)
• Concerns regarding the use of CODM to identify information to be disclosed	• Require disclosure of information monitored by KMP (slide 16)
• Expected synergies can be hard to quantify and not comparable if not defined	• Clarify preliminary views about expected synergies (slide 18)

Location of information

Feedback	IASB's observations and decisions
• The information does not conceptually belong to financial statements	• The information can be required in financial statements because it relates to the items recognised in the financial statements
• The information could be forward-looking • Disclosing such information could expose an entity to litigation risks	• Some consider the information not to be forward-looking because it is information about assumptions underpinning a past transaction, not possible future events or transactions • Even if the information is forward-looking, some say it meets the conditions in paragraph 3.6 of the *Conceptual Framework for Financial Reporting* for inclusion in financial statements

Exemption

Preliminary view	Amended proposal
No exemption	An entity may be exempted from disclosing some information **if doing so can be expected to prejudice seriously an entity's objective for a business combination**

Application guidance

The IASB will accompany the exemption with application guidance, which will include:

- Requirements—for example disclosing the reason for applying the exemption for each item of information
- Considerations of when it is appropriate to use the exemption—for example, it would be inappropriate if that information was already disclosed elsewhere

Rationale

- Address concerns regarding harm that may be caused by commercial sensitivity that might arise from a range of sources—for example, competitors using the information
- Address some elements of concerns regarding litigation risk—for example, if the risk arises because an entity failed to meet an objective as a result of the disclosure

Strategically important business combinations

Preliminary view	Amended proposal
Require an entity disclose information about performance for those business combinations that are monitored by an entity's **CODM**	Require an entity disclose information about the performance of business combinations that are **strategically important**

Thresholds	
Qualitative thresholds—Revenue, operating profit and assets of acquired business constitutes at least 10% of the acquirer's comparative amounts	**Qualitative thresholds**—business combination results in entity entering a new geographical location or a new major line of business

Rationale

- Users will receive information about the most important business combination
- Focusing on a subset of business combinations helps to reduce the cost of disclosing the information
- More targeted identification of business combinations compared to the IASB's preliminary view

Summary of key disclosure decisions

	All material business combinations	**Only 'strategically important' business combinations**
Proposed exemption applies	In year of acquisition, quantitative information about expected synergies	In year of acquisition, information about management's objectives and targets Subsequently, a qualitative statement of whether actual performance met the entity's objective and target
No proposed exemption	In year of acquisition, strategic rationale for undertaking the business combination	Actual performance in subsequent periods

Identifying information to be disclosed

Preliminary view	Amended proposal
Require an entity to disclose information about the performance of a business combination based on information monitored by the entity's **CODM**	Require an entity disclose information based on what is monitored by the **key management personnel**, as defined in IAS 24 *Related Party Disclosures*

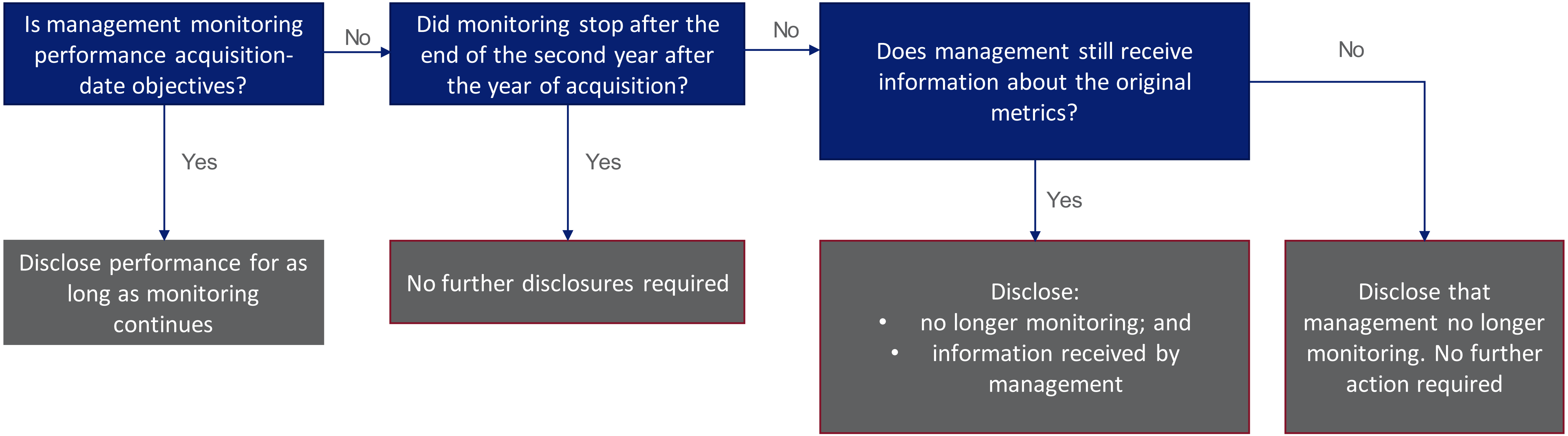
Rationale

- Retains benefits of CODM approach:
  - Focuses on information provided to senior management. This is most likely to be the information relevant to users and information; and
  - Uses an existing term
- Avoids drawbacks of CODM approach:
  - Not associated with segment reporting; and
  - More adaptive to entities with different reporting structure

Duration of disclosure

In considering how long an entity should be required to disclose information about the performance of its strategically important business combinations, the IASB seeks to achieve a balance between:

- Ensuring users receive information about a business combination for a reasonable amount of time; and
- Preparers not being required to disclose the information indefinitely



Expected synergies

Preliminary view
Require an entity to disclose quantitative information about synergies expected from a business combination

IASB's proposal	Rationale
• Require an entity disclose quantitative information about expected synergies	• Academic evidence and feedback suggest that the information is useful and many entities are already providing the information • Concerns from preparers about commercial sensitivity are dealt with by proposing an exemption in specific circumstances (see slide 13)
• Information to be required in year of acquisition only	• Feedback from stakeholder suggests it might be difficult for an entity to follow up on the achievement of synergies
• Not to define expected synergies	• Review of information suggests there is common understanding of 'synergies'
• Allow an entity to disclose range rather than precise amount	• Entities often do not calculate the precise amount of expected synergies

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Other questions

Question	Response
What if the acquired business is integrated with the existing business?	If integration is planned, the entity's objectives, targets and metrics might be about the combined business rather than the acquired business in isolation An entity would not be required to directly attribute the performance of a combined business to pre-existing and acquired businesses
Would the information required by the IASB's proposals be auditable?	Most auditors said the information would be auditable at additional cost. The IASB expects an auditor would be able to verify : • whether the information disclosed is information management receives to monitor the business combination; and • whether there is adequate explanation of how the information has been prepared
Why is the IASB requiring this information only for business combinations and not other types of transactions?	The project began in response to PIR of IFRS 3, where we heard users rely on information from impairment test to understand the success of a business combination Feedback suggests business combinations can be a riskier form of investment

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