IFRS

STAFF PAPER

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IASB® Meeting

Project	**Goodwill and Impairment**		
Paper topic	Better disclosures – feedback from consultative groups		
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Purpose

1. The purpose of this paper is to summarise the feedback received from the Board's consultative groups on the staff's ideas for improving disclosures.

Feedback from the Board's consultative groups

2. Since October 2018, the staff have conducted outreach to obtain feedback on the ideas the staff have been developing to identify better disclosures for business combinations.

3. Meetings were held with the Board's consultative groups, the Capital Markets Advisory Committee (CMAC), the Global Preparers Forum (GPF) and the Accounting Standards Advisory Forum (ASAF).

4. This paper is an extract of the notes of the November 2018 CMAC and GPF meetings and of the December 2018 ASAF meeting relating to the discussions of the staff's ideas for improving disclosures.

Notes of November 2018 CMAC meeting

5. The purpose of this session was to seek CMAC members' feedback on the new disclosure objectives that the Board decided in July 2018 to explore, and on

whether disclosures made with the aim of meeting these objectives can satisfy the needs of users.

6. Specifically, CMAC members discussed the following:

   (a) Additional disclosures at acquisition date

   (b) Why do users need information on the subsequent performance of the acquired business?

   (c) Additional disclosures about subsequent performance

Additional disclosures at acquisition date

7. CMAC members generally agreed that more information is needed to enable them to make a more informed assessment of investment decisions made by management.

8. Members suggested a wide range of disclosures that could help to make information more useful for decisions. Among these suggestions, two types of disclosures gained wide support around the table:

   (a) additional pro forma pre-acquisition information to enhance the comparability of financial information; and

   (b) additional information on the synergies expected from the acquisition to enable users better understand the impact of the acquisition.

Pro forma information

9. Several members stated that additional pro forma information on pre-acquisition financial performance would allow users to see how the consolidated financial statements would have looked if the acquisition had taken place at the beginning of the financial period. Members expressed various views on what information should be provided about financial performance. One member mentioned net earnings (i.e. profit or loss), while another member would like to see all the new subtotals introduced by the Primary Financial Statements project. A few members commented that in addition to information on financial performance, they would also like to see additional pro forma information relating to the acquirer’s financial position and cashflow.

10. One member highlighted that, under current disclosures, users would need to wait close to 3 years after a mid-year acquisition before fully comparable year-on-year financial information is required to be available. Another member mentioned that the standards currently only require disclosure of pro forma revenue and profit and stated that this is insufficient to enable users to analyse the acquisition in detail.

11. One member stated that a newly acquired business is essentially the converse of a discontinued operation to which IFRS 5 Non-current Assets Held for Sale and Discontinued Operations applies. According to the member, pro forma information on the acquired business for the comparative period provides a baseline that allows the subsequent performance of the group to be better understood.

Expected synergies

12. Many members stated that having additional information on the nature, timing and amount of expected synergies would allow users to better understand the transaction, forecast the entity's financial performance and monitor stewardship.

13. One member stated that disclosure on the nature of the synergies (revenue vs cost) is needed to enable users understand how reliable the information is. In his view, estimates of economic benefits from cost synergies are generally more reliable than estimates of those from revenue synergies. Another member stated that quantitative disclosures on expected synergies are more reliable if they are in audited financial statements.

Other comments

14. One member commented that users would need qualitative information on the post-acquisition integration strategy to enable them to monitor the progress of integration and assess the success of the acquisition.

15. In addition, a few members stated that they would like to see additional disclosure on pension and debt obligations taken on by the acquirer in the acquisition. One of them further stated that he would like to know the amount of recourse debt assumed in a business acquisition.

16. A few members also highlighted that the acquired businesses generally have a risk profile different from that of the entity's existing operations. Additional information on the subsequent performance of the acquired business is therefore needed to enable users to better understand the acquisition.

Why do users need information on the subsequent performance of the acquired business?

17. Feedback from CMAC members indicated that information on the subsequent performance of the acquired business is generally needed for 2 purposes:

    (a) To monitor the stewardship of management in making acquisition decisions; and

    (b) To enable users to value the combined business more accurately moving forward.

18. Many members agreed that disclosure on subsequent performance is needed for stewardship monitoring purpose. One member highlighted specifically that this information can be used to assess whether the entity is the best owner of the acquired asset or would be better off disposing the asset instead.

Additional disclosures about subsequent performance

19. CMAC members generally agreed that more detailed disclosures on the subsequent performance of the acquired businesses are needed. However, there is no specific information that would be needed for all acquisitions. One member stated that any information that helps users assess the post-acquisition returns would be useful. The exact information needed to make that assessment may vary from deal to deal. A few members also stressed that quantitative disclosures are preferred to boiler-plate qualitative information.

20. Although members generally agreed that additional disclosures on the subsequent performance of the acquired businesses or combined business would be useful, there were different views on how long and how frequently such information should be provided:

    (a) One member suggested such post-acquisition information is needed for only one financial period post-acquisition to enable users to establish a baseline for comparison.

(b) One member stated that the information would be needed for as long as expected synergy arising from the original deal remains unconsumed.

21. A few members agreed with the staff's suggestion that disclosures relating to the subsequent performance of acquired businesses should be based on benchmarks used internally by management.

22. A few members acknowledged that information on the subsequent performance of acquired businesses or combined business in routine acquisitions may not be traceable due to post-acquisition integration of businesses, and that management may not monitor each acquisition separately. However, they would expect that management would at least monitor separately the performance of major acquisitions. Users would need additional disclosures about subsequent performance for these major acquisitions.

23. One member commented that management should also be required to disclose how the subsequent performance of business acquisitions is monitored. If an entity does not monitor its subsequent performance, it should disclose that fact, and investors will be able to act accordingly. The member stated that requiring such disclosure would create an incentive for management to monitor business acquisitions more closely, promoting better corporate governance.

24. A few members commented that information contained in segment reporting alone is insufficient in addressing the information needs of users relating to the subsequent performance of acquired businesses for the following reasons:

(a) Segment information disclosed in financial statements is generally provided at a level higher than that of individual acquisitions. Information contained in segment reporting would not capture acquisition-specific information; and

(b) IFRS 8 currently does not require the disclosure of some specific information for each segment, such as segment operating cashflow, capital expenditure, assets and liabilities.

Notes of November 2018 GPF meeting

25. The purpose of this session was to seek GPF members' feedback on the disclosure objectives and requirements being developed to provide users with more information about a business combination and its subsequent performance.

Pro forma information

26. One member highlighted that it may be costly to provide pro forma information due to the impact of acquisition accounting entries and suggested that the Board would need to ensure any requirements to provide this information are pragmatic.

Monitoring of acquisition success

27. Several members commented that monitoring of acquisition success would require the tracking of the acquired business's performance. Such tracking would be difficult if the acquired business has been integrated into the acquirer's existing business operations.

28. Several members stated that they do not monitor the post-acquisition business combinations in the manner envisaged by the draft disclosure requirements. They noted that if an acquisition is integrated with an existing business new performance targets are set for the combined business. Management performance is measured against these new targets. One member pointed out that the basis for the new targets could be different from the acquisition assumptions and another member pointed out that the subsequent performance could be impacted by external and internal factors other than the performance of the business combination.

29. A Board member stated that the intent behind suggesting a requirement to disclose objectives of the acquired business or combined business and their subsequent achievement is to hold management accountable for the consideration they paid in an acquisition and provide information that will help users to assess stewardship of management.

30. A few members agreed with the Board member that there was a need to improve the information for investors. They commented that management needed flexibility to tailor the disclosures in the light of entity-specific circumstances and

that different acquisitions would need different factors to describe the subsequent performance of the acquired business or combined business.

31. One member commented there needs to be flexibility to allow for the circumstance that management's objective for the acquired business or combined business changes over time. Another member stated that management could provide users with an explanation when there is a change in objectives.

32. A few members also stated concerns that requiring the disclosure on the achievement of acquisition objectives may lead to companies having to disclose sensitive information that may harm the entity's competitive position. One member also commented that the information may be difficult to audit.

33. Two members emphasised that many business acquiring deals are driven by strategic rather than financial objectives. The subsequent achievement of these objectives could be hard to quantify.

34. Two members commented that additional disclosure should be required, if at all, only for material acquisitions rather than all acquisitions.

35. One member commented that there was no conceptual difference between the acquisition of assets and the acquisition of a business, and thus there is no reason to disclose additional information for the business combination.

Quantitative disclosures on synergies

36. Several members expressed concern over requiring quantitative disclosure on expected synergies in an acquisition because:

    (a) costs of collecting the necessary information for disclosure can be high;

    (b) the information could be commercially sensitive; and

    (c) it is often hard to assign values to expected synergies.

37. One member emphasised that the Board should not try to use information about goodwill to communicate performance of acquired businesses to users of financial statements. Companies' evaluations of acquisitions are not driven by such accounting perspective.

Notes of December 2018 ASAF meeting

38. ASAF members welcomed the enhanced disclosure requirements in relation to business combinations proposed by the staff during recent meetings of the Capital Markets Advisory Committee (CMAC) and the Global Preparers Forum (GPF). ASAF members had mixed views on the concerns of GPF members about the enhanced disclosure requirements. Specifically, the GLASS member did not share the concerns expressed by GPF members, emphasising that management should be held accountable for the decisions that they have made, and that it is surprising that management may not track or monitor such information.

39. Half of the ASAF members (KASB, FRC, ANC, ARD, EFRAG) expressed support for the staff's proposal for enhanced disclosures relating to business combinations and their subsequent performance. Comments by these members include:

    (a) The KASB member suggested that the proposed disclosures could help users understand the financial effects of business combinations and provide users with some assurance about the recoverability of goodwill. The member also suggested enhancing IFRS 8 *Operating Segments* disclosure requirements to include the carrying amount of goodwill allocated to each segment, as well as disclosing separately the carrying amount of goodwill tested for impairment at segment level, and the carrying amount of goodwill tested at a lower level.

    (b) The FRC member supported the disclosure objectives and stated that the enhanced disclosures would alleviate the pressure on the role of goodwill in providing stewardship information. The member also thought the concerns of GPF members were solvable as long as the requirements are not prescriptive and rely on the preparer to state the objectives of the business combination and how these are met over time.

    (c) The ANC member agreed with the enhanced disclosures but thought that the proposals were missing management's final conclusion and justification of the carrying amount of the goodwill.

(d) The ARD member commented that enhanced disclosures would prompt management to exercise more caution when preparing forecasts, which would in turn lead to more timely recognition of goodwill impairments. However, the member further commented that auditors have expressed concerns that the proposed disclosures may contain sensitive information and may not be easily verifiable.

(e) The EFRAG member also agreed with taking an objective-based approach with flexibility to accommodate different acquisition strategies.

40. Some ASAF members, (ASBJ, OIC and some members of the AOSSG) shared concerns similar to those expressed by GPF members:

(a) The ASBJ member commented that companies update their KPI targets regularly and do not focus on the initial acquisition targets for their internal monitoring purposes and that they believe information on the subsequent performance of business combinations should be part of the management commentary.

(b) The OIC member thought the information would be sensitive and difficult to track.

(c) Some members of AOSSG expressed support for disclosures on subsequent performance but were concerned with the feasibility and cost of implementing the proposals. One AOSSG member suggested further outreach should be performed to understand the information entities could provide and some AOSSG members also thought the information should be part of the management commentary.

41. There were mixed views on whether the disclosures should be required only for some fundamental acquisitions. Specifically:

(a) The GLASS, FASB and AcSB members suggested assessing the materiality of the acquisition in the wider context of the corporate strategy. If the corporate strategy leads to a series of acquisitions, these acquisitions should be considered in aggregate.

(b) The EFRAG member commented that the focus should be not on the materiality of the acquisition, but rather on the materiality of the resulting disclosures.

(c) The OIC member commented that it is already difficult to make materiality judgements and cautioned against introducing another level of materiality.

(d) The FRC member commented that the disclosure required should be proportionate to the significance of the acquisition.

42. ASAF also discussed the further disclosure idea which would require entities to disclose its equity and profit or loss excluding the financial impacts of acquired intangible assets that would not be recognised if they had been generated internally and goodwill. ASAF member comments included:

(a) The ARD and the FRC disagreed with this idea because they were of the view that such information can be derived from information that is already available in the financial statements. The FRC member also commented that the disclosure may provide a solution for only some investors because different investors make different adjustments.

(b) The EFRAG member noted that the disclosure would require an entity to determine which acquired intangible assets would have qualified for recognition if they had been generated internally. That member suggested that there may be some practical difficulties in doing this because it would be difficult to avoid applying hindsight in assessing whether future economic benefits are probable.

(c) The AOSSG member commented that AOSSG members had mixed views on the usefulness of these further disclosure items.