Meeting Notes—Joint CMAC and GPF Meeting

The Capital Markets Advisory Committee (CMAC) and Global Preparers Forum (GPF) held a joint meeting on 13 and 14 June 2019 at the London offices of the International Accounting Standards Board (Board).

Members discussed the following topics:

- Disclosure of Sensitive Information (paragraphs [1–6])
- Goodwill and Impairment (paragraphs [7–14])
- Primary Financial Statements (paragraphs [15-25])
- Business Combination Under Common Control (paragraphs 26–33])
- Management Commentary (paragraphs [34–48]); and
- Targeted Standards-level review (paragraphs [48–81])

Disclosure of Sensitive Information

1. The purpose of the session was to seek feedback from CMAC and GPF members on:

    a) whether preparers and investors have a common understanding about characteristics that would help to define sensitive information, or whether that understanding would depend on facts and circumstances;

    b) the kind of sensitive information that investors need and the reasons for requiring such information, and whether preparers can provide the sensitive information that investors need; and

    c) advice for the Board on balancing the needs of investors and the concerns of preparers in future standard-setting activities.

2. Both GPF and CMAC members acknowledged that the sensitivity of information is jurisdiction-, industry- and company-specific. Whilst members did not find a common definition for sensitive information, they agreed that:

    a) the more detail provided; the more sensitive the information was likely to be;

    b) details of negotiations in progress are normally commercially sensitive;

    c) negative news that suggests actual reduction in the future cashflow of the company can be distinguished from information that does not suggest a decrease in future cashflows, but may trigger a negative market response; and

    d) the sensitivity of information is fundamentally about the transparency and investors' trust in management.

3. CMAC and GPF members disagreed regarding the need for disclosures about sensitive information. Specifically:

    a) some GPF members suggested that information included in the examples would be sensitive. They said the counter arguments for requiring the disclosures (set out on the papers) are not valid. Some CMAC members suggested that some information preparers consider sensitive can be gathered through publicly available information. These members were sceptical of claims that such information is sensitive and asserted that disclosure would help investors save costs they would otherwise incur to gather the same information.

b) some CMAC members suggest that companies that disclose the information gain a certainty premium in the market.

4. Some members also observed that existing investors and potential investors may not have aligned interests on the issue of disclosing in sensitive information.

5. Some GPF members suggested those charged with governance, and not the Board, should decide whether companies should disclose sensitive information. However, members agreed that:

a) the Board should avoid taking an extreme view on sensitive information by either ignoring the cost of disclosing the information or by making the disclosure of such information voluntary; and

b) some form of a comply-or-explain model could be adopted, though CMAC and GPF members disagree on the specifics of such a model.

Next steps

6. The Board will consider the feedback received from CMAC and GPF members when it deliberates such disclosure requirements in the future.

Goodwill and Impairment

7. The purpose of this session was to discuss:

a) the impact that the following barriers could have on the proposed improvements to disclosures for business combinations:

i. the commercial sensitivity of information; and

ii. the integration of the acquired business post-acquisition; and

b) the possible removal of some disclosure requirements from IFRS 3 Business Combinations.

8. CMAC and GPF members were provided with case studies of possible disclosures on business combinations. The members generally agreed that the sample disclosures were too detailed and might contain information that would be too commercially sensitive to disclose. However, some CMAC members commented that less detailed information may still be useful.

9. Some GPF members commented that information on subsequent performance should be included in the management commentary rather than in the financial statements. GPF members expressed concerns about the auditability of the information; they also said such information could be forward-looking and, therefore, its disclosure risked litigation. Some CMAC members were unconcerned that such information might not be audited.

10. CMAC members agreed that combined information on the performance of the integrated business post-acquisition could be useful. However, they had mixed views on whether the acquired business must be a certain proportion of the integrated business for such information to be meaningful. Some CMAC members said such information would be useful if the acquired business was at least 50% of the integrated business. In contrast, other CMAC members said that the materiality of the acquired business—rather than the acquired

business's proportion of the integrated business—would be decisive in determining the value of such information.

11. Some CMAC members stated that requiring information about the business combination for only two years post-acquisition might be insufficient.

12. CMAC and GPF members were provided with some IFRS 3 disclosure requirements that the staff thought may be able to be removed. CMAC members disagreed with the staff recommendation to remove the disclosure requirement for pro forma information from IFRS 3. CMAC members said such information is useful in their analysis of the business combination. Some GPF members also commented that pro forma information is not costly to produce. CMAC members had mixed views on the other disclosure requirements the staff were considering could be removed. Some mentioned that disclosures relating to the tax deductibility of goodwill and the impact of gains or losses arising from net identifiable assets acquired in past and current business combinations could be useful. Other CMAC members commented that the other disclosure requirements could be removed.

13. Other comments made by members included:

    a) Some CMAC members would find disclosure of the type of synergy arising from a business combination useful (such as capital expenditure and working capital savings).

    b) Some GPF members questioned why additional disclosures were required for business combinations but not for other capital expenditure. Some CMAC members commented that the additional disclosures for business combinations were needed to assess management's stewardship.

    c) Some GPF members questioned how an entity should determine which business combinations the proposed disclosures relating to subsequent performance should be applied to.

    d) Some GPF members reported that the disclosure requirement for business combinations under IAS 34 Interim Financial Reporting was onerous.

Next steps

14. The staff will consider the feedback from members when drafting the discussion paper.

Primary Financial Statements

15. The Board expects to publish an exposure draft on its Primary Financial Statements project by the end of 2019. The purpose of this session was to help develop the illustrative examples, which will be included in the exposure draft.

16. CMAC and GPF members were asked to discuss three examples:

    a) presentation of subtotals in the statement(s) of financial performance;

    b) disclosure of management performance measures; and

    c) disclosure of unusual items.

17. CMAC and GPF members were also asked which other topics should be illustrated by examples in the exposure draft.

Presentation of subtotals in the statement(s) of financial performance

18. Generally, CMAC and GPF members said the illustrative examples of the statement(s) of financial performance are useful.

19. Some members suggested changes to particular line items included in the illustrative examples (for example, entities are unlikely to have a line for travel expenses).

Disclosure of management performance measures and unusual items

20. Generally, CMAC and GPF members said that in the illustrative example, the format of the management-performance-measure reconciliation and the disclosure of unusual items are useful. However, many members commented that they would like these two disclosures to be in a single note because they are related and separating them would be confusing.

Unusual items and other discussions

21. Some GPF members said it would be difficult and costly to disaggregate the total expenses by nature when the primary analysis of expenses is presented by function. A Board member said that the Board will further consider the feedback during the consultation on the exposure draft.

22. Some CMAC members said the following disclosures would also be useful, although they are not required by the project proposals:

    a) the tax and non-controlling interest effect of unusual items;

    b) the attribution of management-performance-measure reconciling items to line items presented within the statement(s) of financial performance; and

    c) cash flow information on management performance measures or unusual items.

23. Some CMAC members said management performance measures should also include some ratios (for example, return on capital) or EBIT or EBITDA, because they are useful measures.

24. One GPF member asked whether companies who do not have any public communication other than the financial statements, for example private companies, can still include management performance measures in their financial statements. A Board member said that the Board may need to consider this case.

Next steps

25. The staff will seek permission to start the balloting process at a future Board meeting. The staff will consider the feedback on illustrative examples in drafting. The Board will consider other feedback when it redeliberates the proposals.

Business Combinations under Common Control

26. The purpose of this session was to seek CMAC and GPF members' views on the benefits and challenges of:

    a) identifying and accounting for any distribution from the receiving entity's equity applying a current value approach to a Business Combination Under Common Control (BCUCC) transaction; and

    b) providing pre-combination (including comparative) information for combining entities applying a form of predecessor approach to a BCUCC transaction.

27. CMAC and GPF members have been divided in four breakout groups for discussing the topics.

Distribution from equity applying a current value approach

28. CMAC and GPF members of two break-out groups re-iterated the view expressed at previous CMAC and GPF meetings that a current value approach should apply if non-controlling shareholders hold 'substantive' or 'significant' ownership interest in the receiving entity (acquirer). This would be the case, for example, if the receiving entity is publicly held. CMAC and GPF

members of one of those groups expressed the view that a current value approach should not be applied if the receiving entity is privately held or if its shares are held by its employees.

29. CMAC and GPF members discussed whether, and how often, a distribution in a business combination under common control affecting non-controlling shareholders happens in practice. CMAC and GPF members of two breakout groups stated there will be regulatory 'protection' of non-controlling shareholders and members of one group stated that even if there is no regulatory 'protection' there will be contractual protection. Consequently, CMAC and GPF members of that group concluded that the question of how information about any distribution should be provided is theoretical and did not express a view on that question. CMAC and GPF members of another group stated the view that an 'overpayment' is not a theoretical but a real question.

30. All breakout groups shared the view that measuring any distribution would be difficult and the resulting number would be highly subjective and uncertain, or even 'dubious' as characterised by CMAC and GPF members of one breakout group. However, groups assigned different importance to measurement uncertainty considerations and hence expressed mixed views on whether information about any distribution should be provided by recognising the distribution or by disclosure only:

    a) CMAC and GPF members of two breakout groups expressed a preference for recognising a distribution. CMAC and GPF members of one of those groups, that also stated that there will be regulatory 'protection' in place, suggested that the recognised number would often be zero. CMAC and GPF members of the other group, that also stated that the question of 'overpayments' is a real question, emphasised that timely recognition of any 'overpayment' is important. CMAC and GPF members of that group also stated that it is most important for users is to receive information about the economics of the deal and about its anticipated effect on the entity's future cash flows. That would help users make their own assessments of whether there is an overpayment.

    b) another breakout group reported a unanimous view expressed by its GPF members that goodwill should not be overstated and if there is any distribution it should be measured and recognised despite any measurement uncertainty involved. CMAC members in that group expressed mixed views. While some of the CMAC members supported recognising a distribution, others stated that they didn't want to see any 'made-up' numbers in the financial statements and expressed a preference towards disclosure.

    c) CMAC and GPF members of the remaining group stated that the question is theoretical; they did not express a view. Nevertheless, CMAC and GPF members of that group commented that the impairment approach to providing information about any distribution was, in their view, non-workable.

Pre-combination information applying a predecessor approach

31. CMAC and GPF members of all the breakout groups generally considered pre-combination information for all combining entities useful for users of the financial statements, in particular for lenders and other creditors and potential equity investors in an initial public offering (IPO). However, CMAC and GPF members of most of the groups expressed their preference for a prospective accounting in primary financial statements and providing pre-combination information for all combining entities in the notes to financial statements. Specifically, members expressed the following views:

    a) Most CMAC members in one breakout group advocated including 'pro-forma' information in the notes to avoid presenting on the face of financial statements 'something that did not exist before in that form'. Consistent with that logic, some of those CMAC members also emphasised that if a newly set up company (Newco) is involved in a combination, no pre-combination information should be provided on the face of financial statements for any of the combining entities. Instead, pre-combination information for all those entities should be provided in the notes. Other CMAC members in that group stated that they could work with pre-combination information for all entities regardless of whether it is provided on the face of financial statements or in the notes. GPF members in that group commented that they could provide combined pre-combination information, including on the face of financial statements, but providing carveout information would be more difficult.

b) CMAC and GPF members of two other groups suggested that this pro forma pre-combination information is useful but should not be presented on the face of general-purpose financial statements. Instead, such information should be provided in the notes or in special purpose financial reports, for example, those prepared in an IPO. Those members noted that pro forma information is typically already required in an IPO prospectus by regulators. Some CMAC members also suggested that lenders and other creditors can typically require an entity to provide additional information under the terms of the lending contracts. Some of the members of those groups also expressed concerns about the complexity and costs of providing pro forma pre-combination information.

c) CMAC and GPF members of the remaining group suggested that users could work with pre-combination information for all entities, regardless of whether it is provided on the face of financial statements or in the notes. However, those members also expressed the view that pre-combination information on the face of financial statements should be provided only in cases when it matters. Some of the CMAC and GPF members of the group raised a concern about the costs of providing pre-combination information while one GPF member stated such information is typically available for internal purposes.

32. GPF members generally considered it feasible to provide pre-combination information for all combining entities if they were separate legal entities. However, they stated that providing pre-combination information would be more difficult and judgmental in the carveout scenario where no separate legal entities existed before the combination. One GPF member also suggested that management would typically use retrospective information about the combination internally.

Next steps

33. The staff will report the input received from CMAC and GPF members at a future IASB meeting and will consider that input in developing recommendations for the Board.

Management Commentary

34. The purpose of this session was to obtain input from GPF and CMAC members on describing in management commentary:

a) an entity's strategy;

b) its culture; and

c) its funding and liquidity.

Entity's strategy

35. All the breakout groups were generally supportive of the staff's proposed three-component description of strategy that is anchored in the entity's longer-term purpose and explains how that purpose translates into the entity's medium-term objectives and shorter-term plans. Some GPF members from one breakout group said that in practice their entities already discussed strategy in a way similar to that proposed by the staff, although not always within the management commentary.

36. Two of the groups strongly emphasised that an entity's strategy, and in particular its purpose, is inextricably linked to the entity's business model, so they should be discussed together. Those groups also suggested that management commentary should identify and discuss changes to an entity's strategy during the reporting period. Two groups expressed the view that it was important to avoid boilerplate descriptions of purpose in management commentary. One breakout group commented that both its CMAC and GPF members agreed with the staff's view that the Board should not prescribe specific timescales to be used by entities when describing strategy across the short, medium or long term.

Culture

37. Three breakout groups discussed whether management commentary should include a separate description of culture, or whether it is enough for insights into culture to be discernible from other content in management commentary. The groups agreed that understanding an entity's culture is important but a separate discussion of culture in management commentary should not be required because it could end up being boilerplate and unhelpful. However, it is important that users can gain insights into an entity's culture through the content of management commentary. One group expressed the view that measures or indicators that give insights into culture will vary between entities, including those within the same sector, and as a result it would be difficult to prescribe measures or indicators related to culture that should be included in management commentary.

38. Some CMAC and GPF members suggested that insights into an entity's culture could be drawn out from the entity's:

    a) reporting on sustainability, health and safety and human rights issues, dependent on the nature of the entity's business;

    b) governance reporting;

    c) description of its strategy in management commentary; and

    d) reporting on its remuneration policies, particularly for the entity's executive management.

39. One breakout group suggested that management commentary should include information needed to evaluate the effectiveness of management's policies which could give insights into the entities' culture rather than just a description of those policies.

Funding and liquidity

40. The staff proposed that the description of an entity's funding and liquidity position and strategy in management commentary should include:

    a) an analysis of the entity's current financial position and available facilities as well as its current ability to generate net cash inflows;

    b) a discussion of the financial resources needed to implement the entity's strategy; and

    c) a discussion of how risks could affect funding requirements.

41. All the breakout groups agreed with the staff's proposals for describing funding and liquidity position and strategy, and GPF members saw no practical impediments to addressing what was in scope of the proposed description. However, one breakout group commented that stress testing of funding adequacy, which was out of scope of the proposed description, would be desirable. Another group expressed the view that the analysis of an entity's funding and liquidity position and strategy should not replicate information included in the financial statements to meet requirements of IFRS 7 Financial Instruments: Disclosures. Instead, it should provide a high-level qualitative description that is consistent with the notes to the financial statements.

42. Three breakout groups emphasised that a description of funding and liquidity strategy in management commentary should address the entity's strategy for surplus cash and explain how that strategy relates to the entity's distribution or reinvestment strategy. CMAC and GPF members also suggested that the description of an entity's funding and liquidity strategy should cover:

a) both short and long-term funding requirements;

b) how financial risks fit in the context of the entity's other risks;

c) how its funding strategy relates to trends in the entity's business cycle which could result in large capital requirements or loss of cashflow; and

d) changes to its funding strategy.

43. One breakout group highlighted that the level of precision of information about an entity's funding requirements decreases as the length of the period discussed increases. A few GPF members asked for further guidance on how to be precise and informative in describing funding and liquidity position and strategy to avoid a boilerplate description. One breakout group commented that an entity's description of its funding and liquidity strategy is likely to be boilerplate if it is not based on information used by management internally.

Next steps

44. The staff will consider the input from GPF and CMAC members in preparing future agenda papers for the Board.

Targeted Standards-level review

45. The purpose of this session was to seek the views of CMAC and GPF members on example disclosures that might satisfy user information needs relating to employee benefits and fair value measurement disclosures. Specifically, members were asked to discuss whether:

a) each example is effective in meeting user information needs.

b) each example would be costly to prepare.

c) any alternative disclosure might meet the same user information need but be less costly to prepare.

d) each example passes the cost-benefit test.

IAS 19 Employee Benefits

General observations

46. A CMAC member noted that all information about defined benefit pension plans is sensitive to assumptions and, consequently, this member wants to see information about plan assets and their returns. It is important for investors to understand, for example, whether reasonable returns can only be achieved with high-risk investments and what would happen if plan assets were to significantly decline.

Example 1a: Expected contributions into the plan

47. Two breakout groups discussed this example.

48. CMAC and GPF members in both groups agreed that information about expected contributions is important and valuable to investors. GPF members added that the cost of providing the information would not be onerous.

49. Members also made some suggestions about how to make the example disclosure more effective:

a) GPF members thought detailed information should only be provided to the date of the next scheme valuation, with a disclosure of average yearly contributions thereafter. These members also said the disclosure should include information about the frequency of valuations and when the next valuation would take place.

b) GPF members said the disclosure should specify whether valuations are performed on a going concern or solvency basis.

Example 1b: Expected future benefit payments from the plan

50. One breakout group discussed this example.

51. CMAC members confirmed that receiving information about the duration of a defined benefit pension obligation is useful. However, they expressed mixed views about the usefulness of the information in the example disclosure. Some CMAC members thought the information was useful. However, some CMAC members would like to see information about the quality of scheme assets as well as, or instead of, the information in the example. These members added that information about cash contributions (see Example 1a above) and scheme assets would enable them to assess a company's ability to meet its pension obligations.

52. GPF members expressed concerns about the example disclosure, with one suggesting that it belonged in the financial statements of the pension scheme rather than those of the company.

Example 2: Wider sensitivity analysis of significant actuarial assumptions

53. One breakout group discussed this example.

54. CMAC members highlighted the importance of sensitivity analysis. However, they said information about the range of possible values is more useful to their analysis than information about the interrelationships between assumptions.

55. GPF members expressed concern about the preparation costs of the example disclosure. They said the disclosure would require actuarial expertise to prepare, and that costs would be driven by the particular assumptions disclosed, the number of schemes a company has, and the number of countries in which a company operates.

Example 3: Information about differences between defined benefit plan valuations

56. One breakout group discussed this example.

57. CMAC members said that if a company has an alternative valuation of its defined benefit pension scheme(s), they want that valuation to be reported in the financial statements. CMAC members noted that differences in valuation methodology can be explained through investor education and should not need to be explained in the financial statements. However, they thought it would be useful for the financial statements to highlight, for example, differences caused by the timing of valuations.

58. GPF members expressed some concerns about providing information on alternative valuations. For example, GPF members noted that alternative valuations are often performed by a third party, such as the pension scheme trustees. Consequently, GPF members said company management could not be accountable for these valuations.

Example 4: Reconciliation from opening to closing balance of the net defined benefit liability (asset)

59. One breakout group discussed this example.

60. CMAC members noted that the reconciliation is useful to their analysis because it enables them to reconcile pension information to the Statements of Financial Position and Performance.

CMAC members added that they would also like to be able to reconcile information to the Statement of Cash Flows.

61. GPF members said that the reconciliation in the example is easy to prepare. However, they said it would not be possible to provide information to enable investors to link information to the Statement of Cash Flows. The members added that it is not possible to extract movements on balances related to pension benefits from overall working capital movements.

IFRS 13 Fair Value Measurement

General observations

62. GPF members said that, in their view:

a) the example disclosures are most important for financial institutions and will often be immaterial to other types of entity;

b) some of the example disclosures relating to Level 3 fair value measurements have the potential to cross into disclosure of sensitive information. For example, detailed sensitivity disclosures could provide information about third party cashflows.

Example 1: Additional disclosures for Level 2 fair value measurements

63. Two breakout groups discussed this example, which contained:

a) a reconciliation between opening and closing balances of Level 2 fair value measurements;

b) information about valuation processes and techniques; and

c) a sensitivity analysis.

64. CMAC members in one breakout group thought the reconciliation between opening and closing balances of Level 2 fair value measurements provided important information. CMAC members in the other breakout group identified transfers between Level 2 and Level 3 fair value measurements as the most important information in the example disclosure. GPF members said companies should consider the need for a reconciliation separately for each type of Level 2 fair value measurement. These GPF members were concerned about needing to disclose high volumes of information if the Board required the example disclosure for all Level 2 fair value measurements.

65. CMAC members in both breakout groups said the example disclosure about valuation processes and techniques contained useful information about Level 2 fair value measurements. One member added that, to meet their information needs, this disclosure needs to capture a high proportion of a company's Level 2 items.

66. With respect to sensitivity analysis, CMAC members in one breakout group thought information in the example about the effect of a 5% movement in inputs was not useful. These CMAC members would prefer to see an analysis of reasonably possible alternatives and a range of potential values. Such an analysis would enable them to understand the underlying variability of the Level 2 fair value measurements. Some CMAC and GPF members said the example needed more explanation to be useful.

Example 2: Explanation of how an entity has determined the level to which its assets and liabilities belong

67. One breakout group discussed this example.

68. CMAC members observed that Level 2 fair value measurements are of varying quality—ie, they cover items with a wide range of measurement uncertainty, with some being closer to Level 1 and others being closer to Level 3. CMAC members' priority is understanding the quality of the measurements in Level 2. For example—what proportion of Level 2 assets are subject to little

measurement uncertainty and are close to the Level 1 boundary? Consequently, CMAC members thought the disclosures in Example 1 (above) were more effective than the disclosures in Example 2 in meeting their information needs about Level 2 fair value measurements.

69. GPF members thought the example disclosure would only be relevant for financial institutions. CMAC members said they want information about Level 2 fair value measurements for some entities outside financial institutions.

Example 3: Wider sensitivity analysis of Level 3 fair value measurements

70. One breakout group discussed this example.

71. CMAC members thought the sensitivity table on slide 25 of the meeting materials provides useful information. They supported disclosure of an overall sensitivity range that shows the extreme positive and negative scenario for each fair value measurement and said this information better meets their needs than disclosure of the effect of percentage movements on individual assumptions. CMAC members added that it would also be useful to understand the primary assumptions used as inputs into the example disclosure.

72. However, CMAC members added that Level 3 fair value measurements are often immaterial. Consequently, though they support disclosure of the information in the example, these members would like to see that information provided for Level 2 fair value measurements.

73. GPF members agreed that the range disclosed in the example provides better information than—and could be prepared at a similar cost as—an assumption-by-assumption analysis.

74. CMAC members also noted that, often, financial institutions have to provide a range of potential fair value measurements to regulatory bodies. They said it would be useful for companies to include that same range in the financial statements. In their view, this would require no additional preparation cost and provide robust information to users of financial statements. It would also give users an understanding of what is in Level 2—the wider the range, the riskier the Level 2 items.

Example 4: Reconciliation from opening to closing balance of Level 3 fair value measurements

75. Two breakout groups discussed this example.

76. CMAC members thought the table in the example contained a useful level of detail and considered it a 'best in class' disclosure. They identified transfers in and out of different levels of the fair value hierarchy as the most individually critical items in the table. They also identified exchange rate movements as critical. CMAC members added that they would like to see the same information for Level 2 fair value measurements.

77. GPF members in one break out group said they can prepare the information in the example, but they questioned whether the level of detail passes the cost benefit test. GPF members in the other breakout group recommended the Board seek feedback about costs from companies who already provide this level of detail in their financial statements.

Next steps

78. The Board will use the feedback received when making decisions about potential amendments to the disclosure requirements of IAS 19 and IFRS 13 over the coming months.

Next meetings

79. The next GPF meeting will be held on 8 October 2019. The next CMAC meeting will be held on 10 October 2019.