Staff paper

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IASB® meeting

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Project	**Goodwill and Impairment**
Topic	**Exemption from disclosure requirements**
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Purpose and structure

1. As noted in Agenda Paper 18A, we think the International Accounting Standards Board (IASB) should explore exempting entities from disclosing information that would be required by the IASB's preliminary views. The preliminary views were included in the Discussion Paper *Business Combinations—Disclosures, Goodwill and Impairment* and are summarised in Agenda Paper 18A.

2. Agenda Paper 18B analyses whether the IASB should exempt entities from disclosing information that would be required by the preliminary views and if so, what items of information that exemption should apply to. This paper analyses:

   (a) how to design an exemption (paragraphs 5–23); and

   (b) application guidance on applying the exemption (paragraphs 24–42).

Key messages

3. The exemption should be designed to allow entities to not disclose a particular item of information in situations in which disclosing that item of information can be expected to prejudice seriously any of the entity's objectives for the business combination.

4. The IASB should supplement the exemption with application guidance, including:

   (a) requiring an entity to:

      (i) consider whether it is possible to disclose information at a sufficiently aggregated level that would resolve concerns while still meeting the objectives of the disclosure requirements;

      (ii) disclose the reason for applying the exemption separately for each item of information; and

      (iii) assess in future periods whether the circumstances leading to the application of the exemption still exist.

   (b) specify situations in which the exemption would not be permitted, including:

      (i) a general risk of a potential weakening of competitiveness due to disclosure is not, on its own, sufficient reason to apply the exemption;

      (ii) the exemption should not be applied to avoid disclosing information only because that information may not be considered favourably by the market;

      (iii) the information is disclosed in other publicly available material; and

(iv) if competitors are already likely to have access to the information from public or non-public documents or other sources, or would be unable to act on the information in a manner that can be expected to prejudice seriously any of the entity's objectives for the business combination.

How to design an exemption

5. As noted in paragraph 10 of Agenda Paper 18B, we think an exemption would best address concerns about the costs of disclosing proprietary information (proprietary costs), in particular concerns about commercial sensitivity. In considering how to design such an exemption we considered:

   (a) Describing the circumstances in which proprietary costs could arise (paragraphs 6–8); and

   (b) Probability threshold (paragraphs 9–13).

Describing the circumstances in which proprietary costs could arise

6. The IASB would need to describe the circumstances in which proprietary costs could arise from an entity disclosing proprietary information. We think there are two ways to identify those circumstances:

   (a) risk of failing to meet the key objectives of the business combination; or

   (b) potential loss in the entity's value.

7. In our view, the IASB should link the circumstances in which an exemption could be applied to the risk of failing to meet the key objectives of the business combination. This is because:

   (a) it would be difficult to define an exemption linked to the potential loss in the entity's value that distinguishes losses arising from disclosing the information and losses that result from other factors such as negative market reaction to the entity's decision to undertake the business combination or wider economic effects. It is possible that entities could apply an exemption linked to loss in the entity's value in situations in which disclosing the information would not be commercially sensitive.

   (b) linking an exemption to the key objectives of the business combination provides a more direct link to the outcome of the specific transaction to which the information relates. This approach is similar to the one the IASB took for the exemption in IAS 37 *Provisions, Contingent Liabilities and Contingent Assets*[1].

   (c) basing an exemption on failure to meet the key objectives of a business combination could address some aspects of concerns about forward-looking information in addition to the concerns about disclosing commercially sensitive inforamtion (paragraphs 16–23).

8. We think the exemption should permit an entity to not disclose a particular item of information if disclosing that information would risk the entity not meeting *any* of the key objectives of the business combination. For example, assume an entity has three key objectives and three targets for a business combination that are each linked to one of the key objectives. We think the entity should be able to apply the exemption and not disclose one of those targets if doing so could result in failure to meet any one of the three key objectives of the business combination and not just the key objective that the target is being used to measure.

[1] Paragraph 92 of IAS 37 exempts an entity from disclosing some or all information that would be required by paragraphs 84–89 of IAS 37 if doing so can be expected to prejudice seriously the position of the entity in a dispute with other parties on the subject matter of the provision, contingent liability or contingent asset that the information relates to.

Probability threshold

9. As reported in Agenda Paper 18A of the IASB's July 2022 meeting, regulators sometimes exempt an entity from providing some information that would otherwise be required by local regulatory reporting if prescribed conditions are met. For example:

   (a) the Australian Securities & Investments Commission allows an entity to not provide information that is likely to result in 'unreasonable prejudice' to the entity. The Australian Securities & Investments Commission published Regulatory Guide RG 247, which explains how that exemption should be applied (ASIC guidance).

   (b) Regulation (EU) No 575/2013 allows an entity to not provide information that is immaterial, or contains proprietary or confidential information. The European Banking Authority published Guideline EBA/GL/2014/14 explaining how that exemption should be applied (EBA guidance).

10. Both the ASIC guidance and the EBA guidance require an entity to consider the likelihood of negative consequences when deciding whether to apply the exemption. The ASIC guidance states that for an entity to apply the exemption, the unreasonable prejudice must be 'more probable than not'. The EBA guidance states that a mere possibility of negative consequence is not sufficient for the use of the exemption.

11. In addition, the exemption in paragraph 92 of IAS 37 permits an entity not to disclose some information required by paragraphs 84-89 of IAS 37 if disclosure 'can be expected to prejudice seriously the position of the entity in a dispute with other parties on the subject matter of the provision, contingent liability or contingent asset'. We think the phrase 'can be expected to prejudice seriously' implies an assessment of the likelihood of serious prejudice occurring.

12. Feedback from ASAF members suggests that the exemption in IAS 37 works well. We think the implicit probability assessment in paragraph 92 of IAS 37 could help an entity assess when the exemption should be applied and could contribute to the feedback that this exemption works well.

13. Consequently, we think the IASB should use similar wording in designing an exemption from disclosing information that would be required applying the preliminary views. In other words, an entity should be allowed to not disclose a particular item of information if doing so 'can be expected to prejudice seriously' any of the entity's objectives for the business combination.

Would the exemption reduce proprietary costs of disclosing information?

14. We analyse two aspects of the proprietary costs of disclosing information:

   (a) commercial sensitivity (paragraph 15); and

   (b) forward-looking information (paragraphs 16–23).

Commercial sensitivity

15. We think linking an exemption to the risk of failing to meet the key objectives of the business combinations would be sufficiently broad to capture various circumstances in which information could be commercially sensitive while being specific enough to ensure it is not applied for more general risks that are unrelated to the business combination. For example, an entity might risk failing to meet the key objectives of the business combination as a result of disclosing particular information about a business combination if:

   (a) the entity's competitors can be expected to use the information disclosed (which they would not otherwise have access to) to prevent the entity from meeting its objectives;

(b) there is a risk of litigation from users of financial statements (users) or other parties and that litigation can be expected to result in the entity not achieving the business combination's objectives; or

(c) there are legal obligations that prevent the entity from disclosing a particular item of information, the breach of which can be expected to result in legal consequences that would prevent the entity from achieving the business combination's objectives.

Forward-looking information

16. As noted in Agenda Paper 18A to the IASB's October 2021 meeting, we think most of the information that would be required applying the preliminary views is not forward-looking as defined in paragraph 3.6 of the *Conceptual Framework for Financial Reporting* (*Conceptual Framework*). Accordingly, we think an exemption is not needed in relation to the information being forward-looking.

17. However, we understand that others disagree with our conclusion. Also, as noted in Agenda Paper 18B of the IASB's October 2021 meeting, practical concerns about that information being included in financial statements could result from potential differences in the definitions of forward-looking information in jurisdictional requirements and in the *Conceptual Framework*. In particular, we understand that in some jurisdictions, entities are entitled to 'safe harbour' provisions which provide entities with protection from legal action in respect of forward-looking information disclosed in documents other than financial statements.

18. Accordingly, we considered whether the IASB should address litigation risk that might arise from disclosing what some consider to be forward-looking information when designing an exemption. We think litigation in relation to a business combination could arise if (a) an entity disclosed information that some consider to be forward-looking at the time it enters into the business combination (eg objectives); (b) users base economic decisions on that information; and (c) actual performance in future periods differs from the information disclosed initially.

19. An entity may be litigated against for failing to meet its key objectives for a business combination because:

(a) disclosing the information resulted in the entity being unable to meet the objectives of the business combination;

(b) factors outside the entity's control—eg a global pandemic results in significant changes to consumer behaviour; or

(c) management did not efficiently and/or effectively discharge its responsibilities.

20. In our view, litigation risk arising from an entity failing to meeting its objectives for the business combination as a result of disclosing the information (paragraph 19(a)) would and should be addressed by the exemption described in paragraph 13.

21. The litigation risk arising from factors discussed in paragraphs 19(b) and 19(c) results from the entity failing to meet the business combination's objectives for reasons other than the disclosure of the information itself. In other words, it is not the disclosure of information that caused the entity to not achieve its objectives. This risk is, in our view, no different to litigation risk that arises from disclosing 'forward-looking information' that is required by other IFRS Accounting Standards. For example, we think such a risk exists for the measurement and disclosure of expected credit losses applying IFRS 9 *Financial Instruments* or the disclosure of assumptions used in the impairment test required by IAS 36 *Impairment of Assets*.

22. We see no basis to include an exemption to address that risk in relation to the information that would be disclosed applying the preliminary views and not in other circumstances in which that risk arises. In our view, such risks represent general risk of doing business. Although we acknowledge an entity may not

be able to access litigation protection described in paragraph 17, this is also the case for other items of information required by IFRS Accounting Standards today that some consider to be 'forward-looking'.

23. Consequently, we think the IASB should not design an exemption for litigation risk arising from disclosing what some consider to be forward-looking information beyond that which would already be addressed by the exemption described in paragraph 13.

Application guidance

24. To make an exemption more operational, auditable and enforceable, the IASB could include application guidance.

25. To identify possible areas of application guidance, we considered exemptions in IFRS Accounting Standards, exemptions in the Integrated Reporting Framework (IR Framework) published by the International Integrated Reporting Council, exemptions from regulatory reporting requirements and feedback from Accounting Standards Advisory Forum (ASAF), Capital Markets Advisory Committee (CMAC) and Global Preparers Forum (GPF) members. See paragraphs 38–46 of Agenda Paper 18A to the IASB's July 2022 meeting for further information about our research.

26. We analysed:

    (a) disclosing information at an appropriate level of detail (paragraph 27–29);

    (b) disclosing the reason for the application of the exemption separately for each item of information (paragraphs 30–32);

    (c) the frequency in which the exemption is expected to be applied (paragraphs 33–34);

    (d) continuous assessment (paragraphs 35–38); and

    (e) specifying situations when an entity may not apply the exemption (paragraphs 39–41).

Disclosing information at an appropriate level of detail

27. The IR Framework exempts entities from disclosing information that 'would cause significant competitive harm'. Applying the IR Framework, an entity is required to consider 'how to describe the essence of the matter without identifying specific information that might cause a significant loss of competitive advantage'.

28. As noted in paragraph 42 of Agenda Paper 18A to the IASB's April 2022 meeting, some preparers said disclosing information at the level illustrated in our staff examples would generally not be commercially sensitive but highlighted specific information within those examples that they viewed as being commercially sensitive.

29. We think feedback on the staff examples highlights that it might be possible to disclose the information that would be required by the preliminary views in a way that does not result in the disclosure of commercially sensitive information. Accordingly, we think the IASB should include as application guidance a requirement for an entity to consider whether it is possible to disclose the required information at a sufficiently aggregated level that would resolve the concerns while still meeting the objectives of the disclosure requirements before applying the exemption.

Disclosing the reason for the application of the exemption separately for each item of information

30. If an entity applies the exemption in paragraph 92 of IAS 37, that paragraph requires an entity to disclose 'the fact that, and reason why, the information has not been disclosed'. We think it would be helpful for the exemption to include a similar requirement.

31. At previous IASB meetings, one IASB member suggested requiring an entity using an exemption to disclose separately the reason it is using the exemption for each item of information it would otherwise be required to disclose. In that IASB member's view, this would prompt management to carefully consider whether the exemption is required, potentially helping to prevent boiler plate disclosures.

32. We agree and think the IASB should require an entity to explain the application of the exemption for each item of information it applies the exemption to. For example, if an entity has 3 key objectives for a business combination, with separate corresponding metrics and targets, the entity will need to disclose the reason for applying the exemption separately for each key objective, metric and target it applies the exemption to.

Frequency in which an exemption is expected to be applied

33. The IASB could include a statement about how frequently it expects the conditions for applying the exemption would be met in practice. There are precedents for including such an expectation, for example, paragraph 92 of IAS 37 states that application of the exemption described in paragraph 7(b) will be in 'extremely rare cases'.

34. However, we think the IASB should focus on identifying the appropriate circumstances in which the exemption could apply and design an exemption that will be applied in only those circumstances. We think assessing whether those circumstances exist (and how frequently they arise) is better left to preparers, auditors and regulators.

Continuous assessment

35. We think some of the circumstances that stakeholders identify as causing information to be considered commercially sensitive could exist for only a limited period of time. Disclosing information after that period would no longer be expected result in the entity not being able to achieve the objectives of the business combination.

36. For example, if an entity's objective is to launch a new product, the disclosure of that objective could result in the entity not being able to successfully launch the product and therefore could risk the entity not achieving its objective. However, after the new product is launched, that information becomes public knowledge and therefore could no longer harm the achievement of the objective if disclosed.

37. Some jurisdictions impose continuous disclosure obligations that require an entity to the assess the commercial sensitivity of information on a continuous basis. For example, Chapter 3 of the Australian Stock Exchange listing rules stipulates that an entity may be exempted from disclosing some information if the disclosures contain certain commercially sensitive information. If the information ceases to be commercially sensitive subsequently, the entity is required to immediately disclose that information.

38. We think the IASB should include similar requirements for entities applying an exemption. The IASB could require an entity to reassess at each reporting date whether the circumstances which caused an entity to apply the exemption in a prior period continue to exist. If the circumstances no longer exist, the entity would no longer be able to apply the exemption and would be required to disclose that information.

Situations in which an entity cannot apply the exemption

39. The ASIC and EBA guidance referred to in paragraph 9 describe circumstances in which concerns about negative consequences are assumed not to exist and therefore where applying the exemption would be inappropriate.

40. Examples of circumstances in which negative consequences are assumed not to exist include:

    (a) the disclosure of information that is already contained in continuous disclosure notices, investor presentations, briefings to analysts or other publicly available documents is unlikely to give rise to unreasonable prejudice to the entity (ASIC guidance);

    (b) in assessing the usefulness of information to competitors, consideration should be given to whether competitors are already likely to have access to the information from public or non-public documents or other sources, as well as the ability of competitors to act on the information to cause significant detriment to the entity (ASIC guidance);

    (c) a general risk of a potential weakening of competitiveness due to disclosure should not, on its own, be seen as sufficient reason for avoiding disclosure. Specific reasoning should be available and should be based on an analysis of the incidence of disclosure of proprietary information (EBA guidance); and

    (d) the disclosure waiver related to proprietary information should not be used to avoid disclosing information that would disadvantage an institution in the market because that information reflects an unfavourable risk profile (EBA guidance).

41. As noted in paragraph 45 of Agenda Paper 18A to the IASB's July 2022 meeting, we are unaware of comprehensive research on the effectiveness of guidance described in paragraph 40. However, we think the IASB should consider including a similar list of circumstances in which information is assumed not to be commercially sensitive when developing an exemption from disclosing that information that would be required applying the preliminary views.

Summary

42. We think the IASB should supplement the exemption with application guidance—paragraph 4 summarises the application guidance we recommend including.