IFRS Accounting

Staff paper

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IASB® meeting

Date	**September 2023**
Project	**Business Combinations—Disclosures, Goodwill and Impairment**
Topic	**Interaction with the IASB's project Disclosure Initiative—Subsidiaries without Public Accountability: Disclosures**
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Purpose

1. This paper includes our analysis and recommendations on whether the International Accounting Standards Board (IASB) should require subsidiaries without public accountability to disclose information that would be required by the IASB's tentative decisions in this project.

2. This meeting follows on from the IASB's discussion on this topic in its July 2023 meeting (see Agenda Paper 18C to that meeting). In this paper we have applied the procedures for maintaining the forthcoming IFRS Accounting Standard *Subsidiaries without Public Accountability: Disclosures* (Subsidiaries Standard) as set out in Agenda Paper 31 to this meeting.

3. This paper includes:

   (a) Summary of staff recommendations (paragraph 4);

   (b) Background (paragraphs 5–14); and

   (c) Staff analysis and recommendations (paragraphs 15–55).

Summary of staff recommendations

4. As a result of our analysis in this paper, we recommend the IASB propose:

   (a) requiring eligible subsidiaries[1] to disclose:

      (i) the strategic rationale for undertaking a business combination (paragraphs 18–24); and

      (ii) whether the discount rate used in calculating value in use is pre-tax or post-tax (paragraphs 49–55).

   (b) not requiring eligible subsidiaries to disclose any of the other information that would be required applying the IASB's tentative decisions, including:

      (i) disclosure objectives (paragraphs 15–17);

      (ii) information about the performance of a business combination (that is information about key objectives, targets and subsequent performance of a strategic business combination) (paragraphs 25–31);

      (iii) contribution of the acquired business (paragraphs 32–39);

      (iv) liabilities arising from financing activities and defined benefit pension liabilities (paragraphs 40–43); and

      (v) segments to which goodwill is allocated (paragraphs 44–48).

Background

Subsidiaries without Public Accountability

5. In July 2021, the IASB published the Exposure Draft *Subsidiaries without Public Accountability: Disclosures* (Subsidiaries ED). The IASB is expected to issue the Subsidiaries Standard in 2024. The Subsidiaries Standard will permit eligible

[1] The term 'eligible subsidiaries' refers to an entity that meets the requirements to qualify as a 'subsidiary without public accountability' that will be set out in the new IFRS Accounting Standard *Subsidiaries without Public Accountability: Disclosures*.

subsidiaries to apply IFRS Accounting Standards with reduced disclosure requirements.

6. An eligible subsidiary that applies the Subsidiaries Standard will apply the recognition, measurement and presentation requirements in IFRS Accounting Standards and the disclosure requirements in the Subsidiaries Standard. The disclosure requirements in the Subsidiaries Standard will be grouped by the IFRS Accounting Standard to which they relate.

7. The Subsidiaries ED proposed reduced disclosure requirements for IFRS Accounting Standards issued up to February 2021. Subsequent to this, on an ongoing basis, each new or amended IFRS Accounting Standard will include amendments to the Subsidiaries Standard so that the Subsidiaries Standard is maintained.

8. Agenda Paper 31 to this meeting explains how the Subsidiaries Standard should be maintained as a result of changes to other IFRS Accounting Standards.

9. As explained in that paper, to maintain the Subsidiaries Standard, the IASB is expected to apply a set of principles when considering whether new or amended disclosure requirements in IFRS Accounting Standards should be reflected in the Subsidiaries Standard. Users of eligible subsidiaries find information about the following useful:

   (a) short-term cash flows, obligations, commitments and contingencies;

   (b) liquidity and solvency;

   (c) measurement uncertainty;

   (d) accounting policy choices; and

   (e) disaggregation of amounts.

10. As noted in Agenda Paper 31 to this meeting, when assessing amendments to the Subsidiaries Standard, the IASB also considers:

(a) a global assessment of the relative costs and benefits of revised disclosure requirements for eligible subsidiaries to ensure that the Subsidiaries Standard meets the needs of users of eligible subsidiaries while also being sufficiently appealing to subsidiaries themselves, so they can benefit from the cost savings associated with applying the Subsidiaries Standard; and

(b) when amending paragraphs in IFRS Accounting Standards that are not included in the Subsidiaries Standard, the reason the IASB previously decided not to include that disclosure requirement.

11. This paper considers amendments to the Subsidiaries Standard in respect of the disclosure requirements the IASB has tentatively decided to include in an exposure draft in its Business Combinations—Disclosure, Goodwill and Impairment project.

12. For the purpose of discussions in this paper, we assume that the Subsidiaries Standard has already been issued, based on the Subsidiaries ED and tentative decisions made by the IASB on the Subsidiaries project to date.

Past discussion

13. In July 2023 the IASB tentatively decided to propose the Subsidiaries Standard be amended to require an eligible subsidiary to disclose quantitative information about expected synergies, subject to the same exemption proposed for an entity applying IFRS 3 *Business Combinations* in the project on Business Combinations—Disclosures, Goodwill and Impairment.

14. The IASB still needs to decide whether and, if so, how to amend the Subsidiaries Standard for other tentative decisions it has made in the Business Combinations—Disclosures, Goodwill and Impairment project.

Disclosure objectives

15. In September 2022 the IASB tentatively decided to propose adding two new disclosure objectives to IFRS 3 that would require an entity to disclose information to help users of financial statements understand:

    (a) the benefits that an entity expected from a business combination when agreeing the price to acquire a business; and

    (b) the extent to which an entity's objectives for a business combination are being met.

16. In April 2023 the IASB tentatively decided not to include disclosure objectives or guidance on how to apply disclosure requirements in the Subsidiaries Standard. Paragraph 17 of Agenda Paper 31A to that meeting states:

    > Whilst acknowledging the views of respondents that support retaining the disclosure objectives, an eligible subsidiary applying the draft Standard is not prohibited from providing disclosures required by IFRS Accounting Standards to comply with the fair presentation requirements in IAS 1 [*Presentation of Financial Statements*]. The IASB's view [in the Subsidiaries ED] was that including the disclosure objectives may compel an eligible subsidiary to provide the same disclosures as if they had not applied the draft Standard, which would be contrary to the project objective.

17. Accordingly, we recommend the IASB propose not including the new disclosure objectives in the Subsidiaries Standard.

Question 1—Disclosure objectives
1. Do IASB members agree with our recommendation in paragraph 17?

Strategic rationale for undertaking a business combination

18. Paragraph B64(d) of IFRS 3 *Business Combinations* requires an entity to disclose the primary reasons for a business combination. In September 2022, the IASB tentatively decided to propose replacing this requirement with a requirement to disclose the 'strategic rationale for undertaking the business combination'.

19. As noted in paragraph 24(a) of Agenda Paper 18B to the IASB's September 2022 meeting, we expect an entity's primary reason for a business combination to be similar to its strategic rationale for undertaking the business combination, with the latter providing a closer link to the entity's overall business strategy and management's objectives for the business combination.

20. The Subsidiaries ED did not propose to include a requirement for an eligible subsidiary to disclose the primary reason for a business combination. Three respondents to the Subsidiaries ED suggested adding this disclosure requirement. However, in May 2023 the IASB tentatively decided not to include this requirement in the Subsidiaries Standard for the reasons noted in paragraphs A2.1 of Agenda Paper 31A to the IASB's May 2023 meeting:

> [The IASB] assessed that it did not relate to a recognition or measurement difference, and the IFRS for SMEs Accounting Standard does not require this disclosure requirement.

21. Feedback in the Business Combinations—Disclosures, Goodwill and Impairment project suggests that information about the strategic rationale of a business combination would be useful for users of eligible subsidiaries. In particular, at the joint meeting between the Capital Markets Advisory Committee (CMAC) and the Global Preparers Forum (GPF) in June 2022, some members agreed that an entity should disclose at least some level of qualitative information for all business combinations and that an entity should disclose the strategic rationale for all business combinations.

22. We think disclosing the strategic rationale for undertaking the business combination is essential for all business combinations because the information can provide relevant context for users to understand how the business combination can affect the entity. In the context of the Subsidiaries Standard, information about the strategic rationale for undertaking a business combination would give context to the quantitative information about expected synergies the IASB tentatively decided in July 2023 to require eligible subsidiaries disclose.

23. Feedback from preparers in the Business Combinations—Disclosures, Goodwill and Impairment project also indicates that information about the strategic rationale of a business combination is generally not commercially sensitive or costly to disclose (see paragraph 30 of Agenda Paper 18C to the IASB's April 2021 meeting). Therefore, we consider the benefits of requiring eligible subsidiaries to disclose the strategic rationale of business combinations outweigh the costs.

24. Accordingly, we recommend the IASB propose requiring an eligible subsidiary to disclose the strategic rationale for undertaking a business combination.

Question 2—Strategic rationale for undertaking a business combination
2. Do IASB members agree with our recommendation in paragraph 24?

Information about the subsequent performance of a business combination

25. In September 2022 the IASB tentatively decided to propose adding to IFRS 3 a requirement for an entity to disclose, for its strategic business combinations, information about:

    (a) management's objectives for the business combination;

    (b) the metrics and targets management will use to monitor whether those objectives are being met; and

(c) in subsequent periods, the extent to which management's objectives are being met, using those metrics, for as long as management monitors the business combination against its objectives.

26. There are arguments for requiring an eligible subsidiary to disclose this information, for example information about management's objectives and targets could provide information about:

(a) short-term cash flows; and

(b) measurement uncertainty because that information helps to explain the price paid and therefore the amounts recognised for the assets and liabilities acquired in the business combination.

27. However, those factors are not the primary reason for which the IASB tentatively decided to propose requiring entities to disclose this information and therefore are not the main benefit users would obtain from that information.

28. As noted in paragraph 2.5 of the Discussion Paper *Business Combination—Disclosures, Goodwill and Impairment,* those disclosure requirements would help a user assess management's ability to realise the expected benefits from a business combination and assess whether the subsequent performance of that business combination indicates that management paid a reasonable price for the acquired business. Hence, the main benefit from the proposals is to provide users information to help them assess management's stewardship of the entity's economic resources.

29. The users of an eligible subsidiary's financial statements typically represent creditors and lenders. Those types of users are likely to be more interested in short-term cash flows and information that help them assess the entity's ability to repay amounts owed and are less likely to need to assess management's stewardship of investment capital than users of financial statements of entities with public accountability.

30. In July 2023, one IASB member suggested requiring an entity to disclose information only about an entity's key objectives for the business combination. We understand the intention of requiring an eligible subsidiary disclose that information is because it

would give helpful context to the quantitative information about expected synergies. However, we think requiring information about the strategic rationale for undertaking the business combination (see paragraphs 18–24) would be more appropriate because:

(a) the information about strategic rationale for a business combination was intended to give a wider context for the business combination but information about key objectives form part of a package of information designed to give a user more information about the performance of a business combination;

(b) in September 2022 the IASB tentatively decided to propose requiring information about key objectives for a business combination for only strategically important business combinations. However, information about the strategic rationale for a business combination would be required for all material business combinations. The latter is the same population of business combinations for which other requirements in the Subsidiaries Standard, including quantitative information about expected synergies, would apply to; and

(c) requiring an eligible subsidiary to disclose key objectives for a business combination would introduce complexity. For example, in September 2022 the IASB tentatively decided to propose information about management's objectives for a business combination be required for only strategically important business combinations. We think an eligible subsidiary is likely to have more strategically important business combinations than a consolidated group. Requiring eligible subsidiaries disclose the information could therefore be more onerous at a subsidiary level than at a consolidated group level.

31. As a result of the analysis in paragraphs 25–30, we recommend the IASB propose not requiring eligible subsidiaries disclose information about the subsequent performance of business combinations. We think the costs of doing so would outweigh the benefits.

Question 3—Subsequent performance of a business combination
3. Do IASB members agree with our recommendation in paragraph 31?

Contribution of the acquired business

32. Paragraph B64(q) of IFRS 3 requires an entity to disclose, to the extent practicable, information about the contribution of the acquired business:

    (a) the amounts of revenue and profit or loss of the acquired business since the acquisition date; and

    (b) the revenue and profit or loss of the combined entity for the current reporting period as though the acquisition date had been at the beginning of the annual reporting period (sometimes called pro forma information).

33. This requirement has been the subject of discussion in the Business Combination—Disclosures, Goodwill and Impairment project. As noted in paragraphs 2.72–2.87 of the Discussion Paper, there are mixed views on the cost and usefulness of this disclosure requirement:

    (a) some stakeholders say the information is not useful because it is hypothetical and there is a lack of guidance on how to prepare the information and entities prepare the information in different ways (paragraph 2.74 of the Discussion Paper).

    (b) users say the information, even with its limitations, is useful (paragraph 2.86 of the Discussion Paper).

    (c) some stakeholders say it is costly to produce the pro forma information—for example, because there is a need to align accounting policies. However, others say it is simple to produce. This difference in views could reflect the diversity in how the information is prepared (paragraph 2.75 of the Discussion Paper).

34. The IASB received similar diverse feedback in response to its preliminary view to retain the requirement in paragraph B64(q) of IFRS 3 (see paragraphs 80–81 of Agenda Paper 18D to the IASB's April 2021 meeting).

35. In the Subsidiaries ED the IASB did not propose to require eligible subsidiaries to disclose information required by paragraph B64(q) of IFRS 3. In May 2023 the IASB

considered a suggestion from one respondent to the Subsidiaries ED to require an eligible subsidiary to disclose this information. The IASB tentatively decided to confirm its view in the Subsidiaries ED and not require an eligible subsidiary to disclose this information. Paragraphs A2.23–A2.24 of Agenda Paper 31A to the IASB's May 2023 meeting discuss the reasons for the decision:

> A2.23. In developing the proposed disclosure requirements in the draft Standard, the IASB followed its approach and made exceptions for improvements to disclosure requirements in IFRS Accounting Standards (see paragraph 9 of the paper). Respondents suggesting further deletions or additions to proposed disclosure requirements have not provided:
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> (a) further information on applying the principles for reducing disclosure requirements (see paragraph 8 of this paper); or
>
> (b) sufficient evidence for why such requirements would (would not) provide useful information to users of eligible subsidiaries' financial statements.
>
> A2.24. The staff also note that:
>
> …
>
> (b) paragraph BC422(c) of the Basis for Conclusions on IFRS 3 explains that the disclosure requirement in paragraph B64(q) of IFRS 3 is primarily intended for public business entities.

36. In November 2021 the IASB tentatively decided to propose amendments to the requirements in paragraph B64(q) of IFRS 3, this includes:

    (a) replacing the term 'profit or loss' in paragraph B64(q) of IFRS 3 with 'operating profit or loss', which will be as defined in the IASB's Primary Financial Statements project;

(b) explaining the objective of the requirement in paragraph B64(q)(ii) of IFRS 3 without providing guidance on how the information required by paragraph B64(q)(ii) should be prepared; and

(c) specifying in paragraph B64(q)(ii) of IFRS 3 that the basis that an entity applies in preparing the information required by that paragraph is an accounting policy.

37. Some IASB members in the IASB's July 2023 meeting said eligible subsidiaries should be required to disclose the information required by paragraph B64(q) of IFRS 3. Those IASB members said the proposed amendments to that paragraph to specify that profit or loss is operating profit or loss will result in more specific information that would be useful to users of eligible subsidiaries' financial statements. In particular, as a result of the proposed changes to paragraph B64(q) users will be able to forecast short term-cash flows and therefore this information meets one of the principles in paragraph 9 for inclusion in the Subsidiaries Standard. Those IASB members say that information about operating profit or loss provides information about short-term cash flows because:

(a) Combined with information about the revenue of the acquired business, users will be able to determine operating margin, a key input in forecasting future cash-flows.

(b) In March 2021, as part of the Primary Financial Statements project, the IASB tentatively decided to require an entity to use the operating profit or loss subtotal as the starting point for the indirect method of reporting cash flows from operating activities. Therefore, information about operating profit or loss can be reconciled to information about cash flows from operating activities.

38. However:

(a) As explained in paragraph 10, the purpose of the Subsidiaries Standard is to reduce the cost of financial reporting for eligible subsidiaries by reducing disclosure requirements while applying the same measurement and recognition requirements as entities that apply full IFRS Accounting Standards. As noted in paragraph 33, some stakeholders said information about the contribution of the acquired business is complex and costly to provide. Requiring eligible subsidiaries to disclose this information might result in the Subsidiaries Standard being too costly to apply.

(b) As noted in paragraph 35, the IASB decided in May 2023 not to include in the Subsidiaries Standard a requirement to disclose information about the contribution of the acquired business (as it is currently required by IFRS 3). We have not received new evidence or information in the Business Combinations—Disclosures, Goodwill and Impairment project that contradicts the reasons for the IASB's decision in May 2023.

(c) In the Discussion Paper, the IASB expressed a preliminary view to require an entity to disclose operating cash flow contribution of the acquired business. Paragraph 2.81 of the Discussion Paper states the intention of that preliminary view was to provide information to help users who use cash flow measures in their analysis. In November 2021 the IASB decided not to proceed with that preliminary view because doing so would be costly and that the information would not be useful. It is not clear how information about operating profit or loss would provide useful information about short-term cash flows at a reasonable cost if the IASB previously considered operating profit or loss was insufficient to give users information about cash flows and that its preliminary view was to propose an entity be required to disclose information about operating cash flow information.

39. On balance, we think the costs of requiring an eligible subsidiary to disclose information about the contribution of an acquired business outweigh the benefits. Therefore, we recommend the IASB propose not requiring eligible subsidiaries to disclose information about the contribution of acquired business (as amended by the IASB's tentative decisions in this project).

Question 4—Contribution of the acquired business
4. Do IASB members agree with our recommendation in paragraph 39?

Liabilities arising from financing activities and defined benefit pension liabilities

40. Paragraph B64(i) of IFRS 3 states:

> B64 To meet the objective in paragraph 59, the acquirer shall disclose the following information for each business combination that occurs during the reporting period:
>
> …
>
> (i) the amounts recognised as of the acquisition date for each major class of assets acquired and liabilities assumed.

41. In November 2021 the IASB tentatively decided to propose to remove the term 'major' from paragraph B64(i) of IFRS 3.

42. The equivalent of paragraph B64(i) of IFRS 3 in the Subsidiaries ED uses wording from *IFRS for SMEs* instead of IFRS Accounting Standards. Paragraph 36(g) of the Subsidiaries ED does not use the term 'major'. Paragraph 36(g) of the Subsidiaries ED would require an eligible subsidiary to disclose 'the amounts recognised at the acquisition date for each class of the acquiree's assets and liabilities'.

43. Accordingly, we recommend the IASB does not amend the Subsidiaries ED to reflect the proposed amendments to paragraph B64(i) of IFRS 3.

Question 5—Liabilities arising from financing activities and defined benefit pension liabilities
5. Do IASB members agree with our recommendation in paragraph 43?

Segments to which goodwill is allocated

44. In July 2023 the IASB tentatively decided to propose requiring an entity applying IFRS 8 to disclose the reportable segments in which cash-generating units containing goodwill are included.

45. The Subsidiaries ED notes that eligible subsidiaries are not required to disclose information required by IFRS 8. Paragraph 213 of the Subsidiaries ED states:

> An entity within the scope of this [draft] Standard is not required to apply IFRS 8. If such an entity chooses to disclose information about segments that does not comply with IFRS 8, it shall not describe the information as segment information. An entity choosing to make such disclosures shall describe the basis for preparing and making those disclosures. If an entity chooses to apply IFRS 8, it shall apply all the disclosure requirements in IFRS 8 and shall state that it has applied IFRS 8.

46. Paragraphs 129 and 130(c)(ii) of IAS 36 *Impairment of Assets* contain disclosure requirements that apply if an entity applying the IAS 36 disclosure requirements reports segment information in accordance with IFRS 8.

47. In the Subsidiaries ED the IASB did not propose an eligible subsidiary be required to disclose information similar to that required by paragraphs 129 and 130(c)(ii) of IAS 36 if the eligible subsidiary chooses to apply IFRS 8. Respondents to the subsidiaries ED did not suggest adding such requirements (see paragraphs A16.1–A16.18 of Agenda Paper 31A to the IASB's April 2023 meeting).

48. We recommend the IASB propose:

    (a) not requiring an eligible subsidiary to disclose in which reportable segments the CGUs containing goodwill are included because eligible subsidiaries are not required to apply IFRS 8; and

    (b) consistent with the approach taken for similar requirements in IAS 36, not requiring an eligible subsidiary to disclose in which reportable segments the CGUs containing goodwill are included if that eligible subsidiary reports segment information in accordance with IFRS 8.

Question 6—Segments to which goodwill is allocated
6. Do IASB members agree with our recommendations in paragraph 48?

Discount rate used for cash flow projections

49. In March 2023 the IASB tentatively decided to remove from IAS 36 the requirement to use pre-tax cash flows and pre-tax discount rates in calculating value in use when performing an impairment test. The IASB also tentatively decided to require an entity to disclose whether a pre-tax or a post-tax discount rate was used in calculating value in use.

50. This proposed requirement to disclose whether an entity used a pre-tax or a post-tax discount rate in calculating value in use would add to the requirements in paragraphs 130(g) and 134(d)(v) of IAS 36 to disclose the discount rate(s) applied to cash flow projections.

51. The Subsidiaries ED did not include a specific requirement for an eligible subsidiary to disclose the discount rate used when calculating value in use. However, as noted in paragraphs A16.5–A16.11 of Agenda Paper 31A to the IASB's April 2023 meeting, a number of respondents to the Subsidiaries ED suggested requiring eligible subsidiaries to disclose the information required by paragraphs 134(d)–(e) of IAS 36.

52. In April 2023 the IASB tentatively decided to add to the Subsidiaries Standard an equivalent requirement to that in paragraph 134(d)(v) of IAS 36.

53. We think the IASB should propose requiring an eligible subsidiary to disclose whether the discount rate used is pre-tax or post-tax for the same reasons as the reasons for proposing to require entities applying full IFRS Accounting Standards to disclose that information:

    (a) Entities applying the measurement requirements in IAS 36 previously were required to use a pre-tax discount rate but would be permitted a choice applying the proposed amendments to IAS 36. Therefore, in future it might not be clear to users whether the discount rate used is pre-tax or post-tax and a requirement to disclose whether the discount rate is pre-tax or post-tax would provide useful information.

(b) Entities will have this information and therefore it is not costly to disclose.

54. Information about whether the discount rate used in calculating value in use also provides information about measurement uncertainty and therefore meets one of the principles for setting disclosure requirements in the Subsidiaries Standard (paragraph 9).

55. Therefore, we recommend the IASB propose to require an entity to disclose whether the discount rate used in calculating value in use is pre-tax or post-tax.

Question 7—Discount rate used for cash flow projections
7. Do IASB members agree with our recommendation in paragraph 55?