STAFF PAPER

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IASB® meeting

Project	**Goodwill and Impairment**
Paper topic	Possible ways forward
CONTACT(S)	Dehao Fang fdehao@ifrs.org

Objective

1. This paper explores possible ways forward for the International Accounting Standards Board's (IASB) preliminary views to require entities to disclose information about the subsequent performance of business combinations and quantitative information about synergies expected from business combinations based on feedback from:
   (a) the Discussion Paper *Business Combinations—Disclosures, Goodwill and Impairment*; and
   (b) additional outreach (see Agenda Paper 18A).
2. This paper does not include a staff recommendation and the IASB will not be asked to make any decisions on this matter at this meeting. We will use feedback from this meeting to inform our analysis and develop a staff recommendation.

Structure of the paper

3. This paper is structured as follows:
   (a) Background (paragraphs 5–8);
   (b) Assessing costs and benefits of the preliminary views (paragraphs 9–30);
   (c) Possible alternatives (paragraphs 31–66); and
   (d) Combining alternatives (paragraphs 67–72).

4. The Appendix contains information about some alternatives we have previously included in staff papers but have not considered further in our analysis.

Background

5. The Discussion Paper sets out the IASB's preliminary views on requiring entities to disclose information about the subsequent performance of business combinations and quantitative information about synergies expected from business combinations (paragraphs 9–10 and paragraphs 11–13 of Agenda Paper 18 to this meeting include those preliminary views)[1]. As noted in Agenda Paper 18A to this meeting, feedback on these preliminary views identified four practical concerns:

   (a) commercial sensitivity—that information could contain sensitive information that, if disclosed, could harm the entity;

   (b) forward-looking information—that information could contain information about the future that, if disclosed, could increase litigation risk;

   (c) integration—an entity may not be able to disclose information that is representative of the performance of a business combination if the acquired business is integrated into the entity's existing operations; and

   (d) auditability—some information that would be required by preliminary views may be costly, or impossible, to audit.

6. In September 2021, the IASB asked us to investigate those practical concerns. Agenda Paper 18A to this meeting reports on the additional outreach we performed and the findings of that outreach.

7. In October 2021 the IASB:

   (a) tentatively decided that, based on the *Conceptual Framework for Financial Reporting* (*Conceptual Framework*), information can be required in financial

[1] References to the 'preliminary views' in this paper refer only to the preliminary views on requiring entities to disclose information about the subsequent performance of business combinations and quantitative information about synergies expected from business combinations and not to other preliminary views that were included in the Discussion Paper.

statements about the benefits an entity's management expects from a business combination and the extent to which management's objectives are being met.

(b) discussed possible ways to address or mitigate practical concerns about the preliminary views and noted it would continue redeliberations at future meetings, including whether or not to proceed with some or all of the preliminary views on disclosures as a result of those practical concerns.

8. This paper explores possible alternatives the IASB could consider to address those practical concerns.

Assessing costs and benefits of applying the preliminary views

9. The *Conceptual Framework* provides a framework for assessing the practical concerns described in paragraph 5. In particular, paragraphs 2.39–2.43 of the *Conceptual Framework* describe the cost constraint on useful financial reporting (cost constraint).

10. Paragraph 2.39 of the *Conceptual Framework* states:

> Cost is a pervasive constraint on the information that can be provided by financial reporting. Reporting financial information imposes costs, and it is important that those costs are justified by the benefits of reporting that information. There are several types of costs and benefits to consider.

11. Considering the cost constraint, the IASB should proceed with the preliminary views if the benefits of reporting the information that would be required applying the preliminary views outweigh the costs of reporting that information. If the benefits do not outweigh the costs, the IASB could amend the preliminary views such that the benefits would outweigh the cost—however, if the benefits would not outweigh the costs, even after amending the preliminary views, the IASB should not proceed with standard-setting on this matter.

Costs

12. As discussed in paragraph 5, feedback highlighted four practical concerns about applying the preliminary views. This section considers whether, and if so, how, the IASB should consider those concerns as costs of applying the preliminary views.

13. Paragraph 2.40 of the *Conceptual Framework* states that the cost of providing financial information is mainly associated with the 'collection, processing, verification and dissemination of financial information'. Paragraph BC2.73 of *Conceptual Framework* explains that cost is a 'characteristic of the process used to provide financial information'.

14. In our view, the costs referred to in the *Conceptual Framework* are direct costs of the process used to provide financial information—we think concerns about integration and auditability would be considered as part of the cost constraint:

    (a) *integration:* integrating an acquired business with an entity's existing operations could make the collection and processing of the information needed more difficult and costly.

    (b) *auditability:* concerns about the information that would be required applying the preliminary views being costly or impossible to audit relate to the cost of verifying (auditing) and disseminating that information.

15. We think the *Conceptual Framework* description of 'costs incurred to provide and use' information does not encompass possible economic consequences that could arise from the concerns about disclosing commercially sensitive information or additional litigation risks arising from disclosing forward-looking information. However, we think those concerns cannot be ignored. We think they are 'specific economic effects' of applying the preliminary views which the IASB should consider when developing new requirements. Paragraph 3.80 of the IFRS Foundation's [Due Process Handbook] states:

    > IFRS Standards specify requirements for entities to provide high-quality, transparent and comparable financial information that can enhance financial stability in the global economy. The Board has regard to the effects on financial stability when

> assessing the effects of new financial reporting requirements to the extent appropriate and when relevant. For example, in explaining to a broad stakeholder audience the expected benefits of a new Standard, the Board may consider it useful to explain the link between increased transparency in financial reporting and a potential positive effect on financial stability. The introduction by an IFRS Standard of a current value measurement basis could, for instance, be a circumstance in which the Board concludes such explanation is appropriate and relevant. In addition, while it is generally impossible to quantitively assess the possible broader economic consequences of new financial reporting requirements, the Board may assess specific economic effects when relevant. The Board is not required to make a formal quantitative assessment of the overall effect of a new or amended IFRS Standard. Initial and ongoing costs and benefits are likely to affect different parties in different ways.

16. Accordingly, when assessing the costs of the preliminary views, we think the IASB should consider the costs of applying the preliminary views to include all the practical concerns noted in paragraph 5, as either:

    (a) Practical costs—the cost of collection, processing, verification and dissemination of financial information, including costs arising from practical concerns about integration and auditability.

    (b) Specific economic effects—including potential consequences that may arise from disclosing commercially sensitive information and from additional litigation risk entities might be subject to as a result of disclosing information required by the preliminary views.

Benefits

17. Paragraph 1.2 of the *Conceptual Framework* describes how general-purpose financial reporting could provide useful information to users of financial statements (users). It states:

> The objective of general purpose financial reporting is to provide financial information about the reporting entity that is useful to existing and potential investors, lenders and other creditors in making decisions relating to providing resources to the entity.

18. The Post-implementation Review (PIR) of IFRS 3 identified that users need better information about the subsequent performance of the acquiree. The Discussion Paper sets out the IASB's preliminary views responding to that feedback.

19. Subsequent outreach confirmed users' needs:

    (a) many respondents to the Discussion Paper, including almost all users, agreed that an entity should disclose information about the subsequent performance of business combinations (see Agenda Paper 18C and Agenda Paper 18D to the IASB's April 2021 meeting). Many preparers also said they understand why users need this information.

    (b) in our additional outreach, most users said the information illustrated in the staff examples is needed for their analysis (see Agenda Paper 18A to this meeting).

20. Users said they need the information that would be disclosed applying the preliminary views to help them assess management's stewardship of the entity's economic resources. In particular, that information would help users assess management's ability to identify a business to acquire, negotiate an appropriate price to acquire that business and execute plans for that acquired business' performance.

21. Academic evidence suggests some of the benefits to users are passed on to entities. For example, Leuz and Verrecchia (2000)[2] documented that the entities' commitment to higher levels of disclosure was associated with lower cost of capital, proxied by lower bid-ask spreads and higher share turnover.

[2] Leuz, C. and Verrecchia, R. E. (2000), 'The Economic Consequences of Increased Disclosure', *Journal of Accounting Research*, 38.

Should the IASB proceed with the preliminary views?

22. The IASB should consider the costs (paragraphs 12–16) and benefits (paragraphs 17–21) of applying the preliminary views in determining whether to proceed with those preliminary views. The IASB could:
    (a) proceed with the preliminary views (paragraphs 24–27);
    (b) not require entities to disclose information similar to that described in the preliminary views (paragraphs 28–29); or
    (c) proceed with an amended version of the preliminary views (paragraph 30).
23. This section sets out our initial views on the costs and benefits of the different options and what feedback and arguments might support each option. As noted earlier in the paper, we are not recommending any one of these options at this stage.

Proceed with preliminary views

24. The IASB may decide to proceed with the preliminary views if it concludes that the benefits of applying the preliminary views outweigh the costs. This may be the case if the IASB is satisfied that:
    (a) the information that an entity would be required to disclose applying the preliminary views has significant benefits. As discussed in paragraphs 17–21, most users said they need that information. Requiring entities to disclose that information would be in line with the mission of the IFRS Foundation to ‘bring transparency, accountability and efficiency to financial markets around the world’. In particular:
        (i) users do not consistently get information that allows them to assess the subsequent performance of business combinations.
        (ii) business combinations represent a significant investment (for example paragraph IN1 of the Discussion Paper notes that in 2019 there was in excess of $4 trillion of deals announced) and generally tend to be higher risk than other types of investment (paragraph 3.60 of the Discussion Paper highlights that a significant proportion of business combinations fail to meet their objectives).

(iii) users said this information is needed for stewardship purposes, in particular, to hold management to account for those significant and risky investment decisions.

(b) the costs of disclosing the information are not significant enough to outweigh the benefits because:

(i) the information is available internally (the preliminary views are based on information available to an entity's Chief Operating Decision Maker (CODM)). Therefore, there may not be significant additional cost in preparing the information.

(ii) although some preparers continue to have concerns about the information being commercially sensitive, some other preparers do not have that concern. However, most of these other preparers would likely not disclose that information without being required to do so.

(iii) many participants other than preparers said concerns about additional litigation risk arising from disclosing forward-looking information in financial statements should not, in their view, prevent the IASB from requiring entities to disclose that information.

(iv) most auditors said, in their view, the information is auditable, albeit potentially with some extra cost. Some users said the information should be audited, therefore indicating that the benefit users could obtain from disclosing the information in audited financial statements would outweigh any additional audit costs.

25. The IASB assesses the costs and benefits of amending IFRS Accounting Standards on a case-by-case basis. Sometimes, although acknowledging preparers' concerns, the IASB has concluded that the benefits outweigh the costs and required entities to disclose information in financial statements. For example, the IASB required entities to disclose information about:

(a) revenue contribution by major customers (paragraph 34 of IFRS 8 *Operating Segments*), which some stakeholders said might be commercially sensitive because the information could give key customers an upper hand in negotiations with the entity (paragraphs BC109–BC111 of IFRS 8);

(b) information about remaining performance obligations in customer contracts (paragraph 120 of IFRS 15 *Revenue from Contracts with Customers*) which some stakeholders said could be forward-looking (paragraphs BC348–BC351 of IFRS 15); and

(c) information about nature and extent of risks arising from financial instruments (IFRS 7 *Financial Instruments: Disclosures*) which some stakeholders said:

(i) could be difficult and costly to audit (paragraph BC43 of IFRS 7); and

(ii) would be better located in management commentary rather than financial statements because of the nature of that information (paragraph BC45 of IFRS 7).

26. If the IASB concludes the benefits outweigh the costs and decides to proceed with the preliminary views, the IASB could still take steps to clarify the preliminary views which could mitigate some of the practical concerns. For example, the IASB could develop:

(a) examples illustrating the application of the requirements and the level of detail at which the required information should be disclosed.

(b) application guidance clarifying that entities may disclose a range rather than a point estimate for targets.

27. Some participants in our additional outreach said such clarifications could help mitigate some concerns about the information being commercially sensitive, forward-looking and difficult to audit.

Not require entities to disclose information similar to that described in the preliminary views

28. The IASB could conclude that despite the benefits of disclosing the information that would be required applying the preliminary views, the costs of disclosing that information outweigh those benefits. Accordingly, the IASB could decide to not proceed with the preliminary views and not require disclosure of information about

the subsequent performance of business combinations and quantitative information about expected synergies because:

(a) a few preparers said, in their view, the information illustrated in the staff examples would not be useful. In addition a few users said they doubted whether the information disclosed by entities would be useful and that they already receive some information about management's expectations for a business combination outside financial statements.

(b) the IASB heard about the practical concerns from many preparers. Therefore, one specific practical concern, or a combination of them could indicate there are significant costs associated with the preliminary views. For example:

(i) disclosing commercially sensitive information could potentially restrict an entity's ability to meet its objectives for a business combination and thereby be detrimental to users. This cost could be so significant that it would outweigh any benefit users might receive from that information.

(ii) although the benefits of 'safe harbour' protections when disclosing forward-looking information outside financial statements are limited to specific jurisdictions, the effect of those protections highlights that the costs of disclosing that information in financial statements would outweigh the benefits for at least those jurisdictions[3].

29. Not requiring entities to disclose information similar to that described in the preliminary views would mean not responding to feedback from the PIR of IFRS 3 suggesting users need better information about business combinations. However, even if the IASB decides not to continue with the preliminary views it could include some requirements in IFRS Practice Statement 1 *Management Commentary*. However, not all entities applying IFRS Accounting Standards are required to, or choose to, apply the Practice Statement. Therefore, this approach may not provide users with better

[3] We understand that some jurisdictions have statutory 'safe harbour' provisions that protect entities from litigation risks that may arise from forward-looking statements. Generally, entities would need to include those forward-looking statements, accompanied with cautionary statements, in management commentary in order to benefit from such 'safe harbour' provisions.

information unless those requirements are also included in local regulatory requirements.

Amend preliminary views

30. The IASB could also conclude that there are significant benefits of disclosing the information that would be required by the preliminary views. However, the IASB could conclude that feedback, particularly from preparers, demonstrates there are significant potential costs that cannot be ignored. Therefore, the IASB could amend the preliminary views to better balance the costs and benefits of disclosing this information. Paragraphs 31–65 discuss possible ways in which the IASB could amend the preliminary views to:
    (a) continue to meet the project's overall objective—improving the information entities provide to users, at a reasonable cost, about the business combinations that those entities make; and
    (b) better balance the cost and benefit of any requirements.

Possible alternatives

31. We acknowledge the practical concerns raised and consider whether, how and to what extent the alternatives discussed within this section could mitigate those concerns.
32. As explained in paragraph 2.36 of the Discussion Paper, the preliminary views would require an entity to disclose information about the subsequent performance of a business combination that is monitored by the Chief Operating Decision Maker (CODM) for business combinations monitored by the CODM. The IASB's view was that such an approach would help focus on the 'most important information for the most important business combinations' (paragraph 2.38 of the Discussion Paper). As explained in paragraphs 24–27, the IASB could decide to proceed with the preliminary views and therefore continue to use the CODM as described in the preliminary views.
33. In developing possible alternatives, we have put aside the use of an entity's CODM to identify (a) the business combinations for which an entity would disclose information,

and (b) the information an entity would disclose. Some of the alternatives discussed below would require an entity to disclose information reviewed by management. If the IASB decides to pursue such an alternative, we will provide the IASB with further analysis as to how to define management in the context of identifying that information at a later stage, including considering the use of an entity's CODM to define management.

34. In developing alternatives, there are two variables that can be adjusted to better balance the costs and benefits of any proposed requirements:

    (a) the population of business combinations for which information would be disclosed, for example by requiring disclosure of information about only 'significant' business combinations (paragraphs 35–43).

    (b) the amount of information required to be disclosed. This could include for example:

        (i) a comply or explain model (paragraphs 44–51);

        (ii) requiring only qualitative information in the year of acquisition rather than quantitative information (paragraphs 52–59);

        (iii) specifying metrics an entity would disclose (paragraphs 60–65).

Disclosing information about only 'significant' business combinations

35. The IASB could require disclosure about the subsequent performance of business combinations and quantitative information about expected synergies for only 'significant' business combinations rather than for all 'material' business combinations [4]. This would follow an approach similar to that in the Discussion Paper (see paragraph 32) but would use a different method for identifying the 'significant' business combinations.

[4] Paragraph B64 of IFRS does not specify a particular population of business combinations to which it applies. However, paragraph B65of IFRS 3 includes specific disclosure requirements that apply to 'individually immaterial business combinations occurring during the reporting period that are material collectively'. In the rest of this paper, we refer to 'material business combinations' as those that are not 'individually immaterial'.

36. Requiring disclosure of information for only ‘significant’ business combinations could help address preparers’ concerns. For example, a few preparers we spoke to in outreach said the information that would be disclosed applying the preliminary views is commercially sensitive but nonetheless disclosed similar information outside financial statements for particular business combinations. Those preparers explained that there are some business combinations that are so ‘significant’ that information needs to be disclosed to users. In other words, for those preparers, the benefits of disclosing information for those ‘significant’ business combinations outweigh the costs of doing so.

37. The IASB could use a similar argument in pursuing this alternative. However, in this alternative the IASB would specify what constitutes a ‘significant’ business combination. This would limit an entity’s ability to decide which business combinations are of such importance that the benefits of disclosing information similar to that required applying the preliminary views outweigh the costs of doing so. A similar rationale would also apply to concerns about additional litigation risk arising from disclosing forward-looking information—that the benefits of disclosing information for those business combinations outweighs the cost of any additional litigation risk.

38. Requiring information to be disclosed for only ‘significant’ business combinations, could also address concerns about integration (and the associated concern about auditing integrated metrics). The preliminary views seek to provide better information to help users assess the performance of a business combination but the Discussion Paper notes that management might use information about a combined business to understand how a business combination is performing. When an entity undertakes a ‘significant’ business combination, the effect of the business combination on the combined business’ performance is likely to be more obvious. Information about the financial performance of such a business combination is also more likely to be reviewed by management, and therefore be more readily available.

39. As paragraph 2.33 of the Discussion Paper notes, some stakeholders expressed concerns about disclosing information about the subsequent performance of business combinations for all ‘material’ business combinations. They said the volume of

disclosures could be onerous, particularly for entities that undertake many business combinations. Focusing on ‘significant’ business combinations would help respond to this concern by reducing the population of business combinations an entity would disclose information about compared to requiring information to be disclosed for all ‘material’ business combinations.

40. There is precedent for identifying specific transactions that are more ‘significant’ to which additional requirements apply. For example, IFRS 5 *Non-current Assets Held for Sale and Discontinued Operations* defines discontinued operations as a subset of disposals and has specific presentation and disclosure requirements which apply to those discontinued operations.

41. There are some drawbacks to this approach. Although some users said information is needed for only ‘significant’ business combinations, many users said information is needed for all ‘material’ business combinations. Therefore, focusing on ‘significant’ business combinations could mean users do not receive information they need for all ‘material’ business combinations. This approach would therefore be a compromise between preparers and users.

42. This approach could also lead to complexity—it would result in the IASB having three levels of disclosure requirements for different populations of business combinations. IFRS 3 sets out general disclosure requirements for business combinations and paragraphs B65 and B67 of IFRS 3 require specific information to be disclosed for ‘individually immaterial business combinations occurring during the reporting period that are material collectively’. Requiring entities to disclose more information for a group of ‘significant’ business combinations would add a third population of business combinations for which a greater level of disclosure would be required.

43. It may also be difficult for the IASB to specify what constitutes a ‘significant’ business combination. We think there are two basic ways to define ‘significant’:

    (a) a quantitative threshold—for example a business combination in which the acquired business represents more than 5% of the reporting entity’s revenue, profit, total assets or net assets. Setting a quantitative threshold has precedence—for example, paragraph 13 of IFRS 8 requires information to be disclosed about operating segments meeting specific quantitative thresholds. In setting a quantitative threshold, the IASB could consider similar thresholds set by regulators who require entities to disclose specific information about business combinations that meet particular thresholds.

(b) a qualitative threshold—for example requiring information to be disclosed for business combinations that comprise a significant portion of the entity's reportable segments and business combinations that are themselves separate reportable segments. Using a qualitative threshold has precedent in, for example, IFRS 5 which qualitatively defines discontinued operations.

Comply or explain

44. The IASB could adopt a comply or explain approach in which an entity would disclose information based on the preliminary views but in specific situations the entity would be permitted to not disclose some or all of that information. Instead, the entity would explain the reason for not doing so.

45. The IASB adopted a similar approach in IAS 37 *Provisions, Contingent Liabilities and Contingent Assets*, which permits entities to not disclose information about contingent liabilities if doing so may prejudice seriously the entity's position in a legal dispute (IAS 37 exemption). Paragraph 92 of IAS 37 states that such situations are expected to be extremely rare. Respondents suggesting this approach say the IAS 37 exemption is not often used in practice, and therefore the risk of such an approach being abused might be limited.

46. In developing such an exemption, the IASB could design particular criteria that would have to be met for the exemption to apply—these criteria could be broad (allow exemption in a broad range of situations) or restrictive (allow exemption in a narrow set of situations).

47. Depending on the criteria, this approach could help mitigate practical concerns about commercial sensitivity, additional litigation risk arising from disclosure of forward-looking information and/or integration of businesses. For example, the IASB could design criteria to address:

(a) commercial sensitivity—for example, by exempting an entity from disclosing particular information if doing so would reasonably be expected to result in the entity being unable to realise its objective for the business combination.

(b) forward-looking information—for example, by exempting an entity from disclosing particular information in financial statements if doing so would reasonably be expected to result in significant additional litigation risk compared to disclosing that information in other documents.

(c) integration—for example, by exempting an entity from disclosing particular information if it is impracticable to disclose the information because the acquired business has been integrated with the entity's existing business.

48. There is academic evidence on the effectiveness of simple comply or explain approaches, albeit not in the context of IFRS Accounting Standards. For example, Arcot, Bruno and Faure-Grimaud (2010)[5] reviewed compliance with the UK Corporate Governance code, which uses a simple comply or explain approach with no restrictions on when an entity is permitted to explain rather than comply. The authors found an increasing trend of compliance over time, but also found frequent use of standard, boilerplate explanations when the 'explain' option was used.

49. We discussed more generally the disclosure of commercially sensitive information with the IFRS Foundation Advisory Council (March 2019) and at the joint Capital Markets Advisory Committee (CMAC) and Global Preparers Forum (GPF) meeting (June 2019). Some participants said a comply or explain approach could be a practical way to balance the need to provide users better information and preparers' concerns about commercial sensitivity. Such an approach could incentivise an entity to disclose information if the cost is acceptable because the entity risks being penalised by the market if its explanation for not disclosing the information is deemed unsatisfactory. Some respondents to the Discussion Paper also shared similar views. However, some participants highlighted concerns about a comply or explain approach, which include:

(a) the option to avoid disclosing specific information may be abused;

[5] Arcot, S., Bruno, V. and Faure-Grimaud, A. (2010), 'Corporate governance in the UK: Is the comply or explain approach working?', *International Review of Law and Economics*, 30.

(b) the approach could be difficult to apply consistently, particularly when entities operate in different markets and regulatory environments;

(c) the explanation for not disclosing information could itself contain information that could be commercially sensitive or forward-looking, and therefore would not necessarily address the practical concerns; and

(d) the approach would require entities to exercise judgement and could lead to tension among preparers, regulators and auditors.

50. It might be difficult to develop robust criteria that effectively targets specific concerns because of the unique circumstances surrounding each business combination. For example, it might be difficult to define ‘significant additional litigation risk’ (paragraph 47(b)) in a way that is enforceable by auditors and regulators. Furthermore, in developing IFRS 8, the IASB considered whether to exempt entities from disclosing particular information if doing so could cause competitive damage or erosion of shareholder value. The IASB decided not to provide such an exemption because it would provide a means for broad based non-compliance (paragraphs BC43–BC45 of IFRS 8).

51. A few preparers said management is in the best position to assess whether it is in the interest of an entity to disclose particular information about business combinations. In their view, it would be difficult for the IASB to develop specific exemption criteria.

Not require quantitative disclosures in the year of acquisition

52. The preliminary views would require an entity to disclose, in the year of the business combination, quantitative information about management’s key objectives and expected synergies for a business combination.

53. The IASB could allow entities to disclose qualitative information, instead of quantitative information, in the year of a business combination. Under this approach, an entity would be required to disclose, in the year of the business combination, qualitative information about management’s key objectives for a business combination and the metric(s) management will use to monitor whether the objectives of the business combination are being met without disclosing the quantitative target(s)

for the metric(s). In subsequent periods, an entity would be required to disclose the actual result(s) using the metric(s) disclosed in the year of acquisition and whether the target was met.

54. For example, if management's key objective for a business combination is to increase revenue by CU100 million each reporting period, the entity would be required to disclose, in the year of the business combination, only its objective of increasing revenue and that it will use revenue as the metric to measure the success of the business combination—the entity would not be required to disclose its quantitative target of increasing revenue by CU100 million. In subsequent reporting periods, the entity will disclose the actual increase in revenue achieved for that period (say CU98 million) and whether that increase of CU98 million met management's objective. This approach could reduce concerns about:

    (a) additional litigation risk that might arise from disclosing information that some regard as forward-looking—this is because an entity would not be required to disclose forward-looking quantitative information;

    (b) disclosing commercially sensitive quantitative information about management targets in the year of acquisition while still providing users information about the actual subsequent performance of a business combination; and

    (c) the potential expectation gap over the audit of management targets where stakeholders might expect auditors to provide assurance over the reasonableness and appropriateness of management targets—this is because an entity would not be required to disclose quantitative information about those targets in the year of acquisition.

55. During additional outreach with stakeholders, many preparers suggested allowing entities to disclose qualitative information to satisfy the IASB's objective of requiring entities to provide better information about business combinations.

56. However, some preparers did not support this alternative because:

    (a) entities would still be required to disclose, in subsequent financial periods, whether initial targets for a business combination were achieved. This could be challenging because it might be difficult to isolate the performance of an acquired business due to integration (see paragraph 60–66 of Agenda Paper 18A);

(b) auditors might not be comfortable providing assurance on a statement about whether management's targets for a business combination are met without quantitative disclosure of the targets.

57. Many users said they do not like this approach because they would be unable to assess the reasonableness and appropriateness of management's objectives for a business combination if management did not also disclose the quantitative target. This alternative could therefore limit users' ability to understand the reasons for the purchase price, which is one of the disclosure objectives the IASB considered adding to IFRS 3 in the preliminary views.

58. Not requiring entities to disclose quantitative information in the year of acquisition may not fully meet users' needs and would also mean not addressing feedback from users that qualitative information about synergies disclosed by entities applying IFRS 3[6] today is often boilerplate and not useful. There is a risk that additional qualitative disclosures about management objectives could also be boilerplate.

59. In addition, academic evidence (see paragraph 17 of Agenda Paper 18F of the IASB's May 2021 meeting) shows that information about expected synergies in the year of acquisition provides market participants with useful information, and that this information is used as a yardstick to judge the success of a business combination.

Specifying metrics

60. The IASB could also replace the preliminary view of requiring entities to disclose information reviewed by management about business combinations (a management approach) and instead require entities to disclose specific metrics for all business combinations.

[6] Paragraph B64(e) of IFRS 3 requires an entity to provide 'a qualitative description of the factors that made up the goodwill recognised, such as expected synergies from combining operations of the acquiree and the acquirer...'

61. For example, paragraph B64(q) of IFRS 3 requires an entity to disclose information about the revenue and profit[7] of an acquired business in the year of acquisition—the IASB could require an entity to continue to provide this information for a specified period of time after the acquisition. Other examples of metrics suggested by some respondents include:

(a) operating margin;

(b) return on investment or return on capital employed; and

(c) estimated payback period for the investment.

62. Prescribing specific metrics might reduce preparers' concerns about commercial sensitivity and additional litigation risk arising from disclosing forward-looking information because:

(a) information about specified metrics might not be linked to management's strategy; and

(b) no information about management's targets would be provided.

63. However, specifying metrics might increase concerns about integration. An entity might integrate an acquired business into its existing business soon after a business combination and management might not be able to isolate the performance of the acquired business from that of its existing business.

64. The IASB considered prescribing specific metrics when developing the preliminary views (paragraphs 2.19–2.20 of the Discussion Paper). The IASB rejected this approach because in its view, it is not feasible to prescribe a set of metrics that would be applicable for all business combinations. In addition, prescribing specific metrics might require entities to produce, solely for the purpose of financial reporting, information that is not readily available. This would increase the cost of preparation.

65. During additional outreach with stakeholders, many users supported a management approach, saying they appreciated that entities may undertake business combinations

[7] In November 2021 the IASB tentatively decided to replace the term 'profit or loss' in paragraph B64(q) of IFRS 3 with 'operating profit or loss'. 'Operating profit or loss' will be as defined in the IASB's Primary Financial Statements project.

for different reasons and that the IASB could not prescribe metrics that would be applicable to, and be meaningful for, all business combinations. However, some users said they focus on analysing an entity's ability to generate return from business combinations and they would not take management's objectives for business combinations at face value. These users suggested requiring an entity to disclose specified metrics for all material business combinations. In their view, prescribing specific metrics for all material business combinations would provide relevant information and could enhance comparability.

Summary of benefits and drawbacks of the possible alternatives

66. The table below summarises how each of the possible alternatives discussed in paragraphs 34–65 might resolve or mitigate the practical concerns:

Alternative	**Could mitigate concerns about**	**Drawback**
Disclosing information about only 'significant' business combinations (paragraphs 35–43)	• Commercial sensitivity • Forward-looking information • Integration (and related auditability concern)	• Difficult to determine appropriate threshold
Comply or explain (paragraphs 44–51)	• Depends on the scope for possible exemption but particularly relevant for concerns about commercial sensitivity and forward-looking information	• Risk of abuse • Limits usefulness of information provided

Not require quantitative disclosures in the year of acquisition (paragraphs 52–59)	• Commercial sensitivity • Forward-looking information • Some audit concerns	• Would not mitigate concerns about integration • Could create new audit concerns • Limits usefulness of information provided
Specifying metrics (paragraphs 60–65)	• Commercial sensitivity • Forward-looking information	• Specified metric may not be relevant or applicable for the business combination • Could worsen integration concerns

Combining alternatives

67. The IASB could combine some of the alternatives discussed above to maximise the benefits or limit the drawbacks of each individual alternative. We illustrate two possible combinations:

    (a) ‘significant’ business combinations and specific metrics (paragraphs 68–69); and

    (b) ‘significant’ business combinations and comply or explain (paragraphs 70–72).

‘Significant’ business combinations and specific metrics

68. The IASB could develop an approach that would require entities to disclose (a) particular information for ‘significant’ business combinations; and (b) specified metrics for other business combinations. In this approach, the IASB could require:

    (a) for ‘significant’ business combinations, entities to disclose information about the subsequent performance of business combinations similar to that described by the preliminary views and quantitative information about expected synergies; and

(b) for business combinations that are not 'significant', require entities to disclose information about prescribed metrics (for example revenue and operating profit of an acquired business for a particular number of years after a business combination).

69. This alternative could provide users with better information about 'significant' business combinations for which some would say the benefits of disclosing information outweighs the costs (see paragraphs 35–38), while also addressing users' needs for information about other business combinations. By requiring entities to disclose at least some information for business combinations that are not 'significant', this alternative could also partly respond to feedback from some users that the preliminary views would not require entities to provide users with sufficient information when an entity enters into a series of smaller acquisitions.

'Significant' business combinations and comply or explain

70. Feedback indicates that for 'significant' business combinations the benefits of an entity disclosing information about those business combinations' subsequent performance and expected synergies outweighs the costs (see paragraph 36). However, some might say there could be circumstances in which this would not be the case. For example, some might say in rare circumstances the risk of failing to meet an entity's objectives for a business combination and therefore the cost of disclosing commercially sensitive information is so high that it outweighs the benefits of disclosing that information.

71. To address those rare circumstances the IASB could combine a focus on 'significant' business combinations with a comply or explain approach designed to target those rare circumstances. In this approach, the IASB could require entities to disclose information about the subsequent performance of business combinations similar to that described by the preliminary views and quantitative information about expected synergies for 'significant' business combinations but exempt an entity from disclosing that information in those rare circumstances.

72. However, as noted in paragraph 50 it may be difficult to develop robust criteria that effectively targets those rare circumstances.

Question for the IASB
Do IASB members have: 1) a preference as to whether to focus on the population of business combinations or the information disclosed about each business combination (as described in paragraph 34)? 2) comments or questions on the possible alternatives (or combination of possible alternatives) discussed in this paper (paragraphs 35–72)? 3) suggestions for alternatives we have not considered? 4) any other comments or questions?

Appendix—Alternatives not considered further

A1. This section outlines some alternatives we have discussed previously with the IASB but have not considered further in our analysis of how to address the practical concerns discussed in paragraph 5 of this paper. These include:

(a) allowing entities to cross-refer to information in documents outside financial statements (paragraphs A2–A3); and

(b) developing an objectives-based approach similar to that proposed in the Exposure Draft *Disclosure Requirements in IFRS Standards—A Pilot Approach* (Disclosure Exposure Draft) (paragraphs A4–A7).

Cross-referring to other documents

A2. Information incorporated by cross-reference applying an IFRS Accounting Standard is an integral part of financial statements. Allowing entities to include information by cross-reference is therefore unlikely to resolve concerns about including forward-looking information in financial statements or concerns that it might be difficult to disclose and audit information if the acquired business is integrated.

A3. However, allowing entities to incorporate information by cross-reference could address concerns about information being duplicated in financial statements and other documents. The IASB could consider this alternative for this purpose in future decisions.

Developing an objectives-based approach

A4. Agenda Paper 18B of the IASB's October 2021 meeting included our analysis of an objective based alternative, similar to that proposed in the Disclosure Exposure Draft. This approach would result in using feedback obtained from users and other stakeholders to:

(a) set overall and specific disclosure objectives that explain user needs in detail and require entities to apply judgement and disclose all material information that would enable those needs to be met; and

(b) provide examples of information an entity may disclose to satisfy each disclosure objective. In most cases, these items of information would not be mandatory—instead, they would help entities determine how to meet the required objective.

A5. This approach could provide an entity with flexibility to present information in a way that would minimise any additional litigation risk while still meeting the disclosure objectives and providing useful information.

A6. Some users said entities often provide quantitative information outside financial statements about management's objectives for a business combination, but rarely provide information regarding the achievement of those objectives in subsequent periods. The IASB could explain that an entity can meet this user need (a disclosure objective) by, for example, providing an update in subsequent periods on information disclosed outside financial statements at the time of a business combination.

A7. We have not considered this alternative further because:

(a) although entities would have flexibility in meeting the objectives they would still be required to disclose sufficient information to help users understand the benefits expected from the business combination and the extent to which management's objectives are being met—information that stakeholders say is subject to practical concerns discussed in paragraph 5.

(b) it could have a significant effect on the project timeline. This is because:

(i) IFRS 3 has some disclosure objectives and requirements that were developed before the approach proposed in the Disclosure Exposure Draft was developed. We think if the IASB were to consider this alternative, it would need to also consider whether to apply the same approach and be consistent across all disclosure requirements (existing and proposed) in IFRS 3. This could mean reconsidering existing disclosure requirements, which would widen the scope of the project.

(ii) the Disclosure Exposure Draft was open for comment until 12 January 2022. The IASB may wish to consider feedback from that Exposure

Draft before deciding whether, and if so, how, to follow a similar approach for this project.