



2023

# World Standard-setters Conference

#WSS2023

**Better information  
for better decisions**

## **Business Combinations— Disclosures, Goodwill and Impairment**

Breakout session 5



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## Presenters



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## Agenda

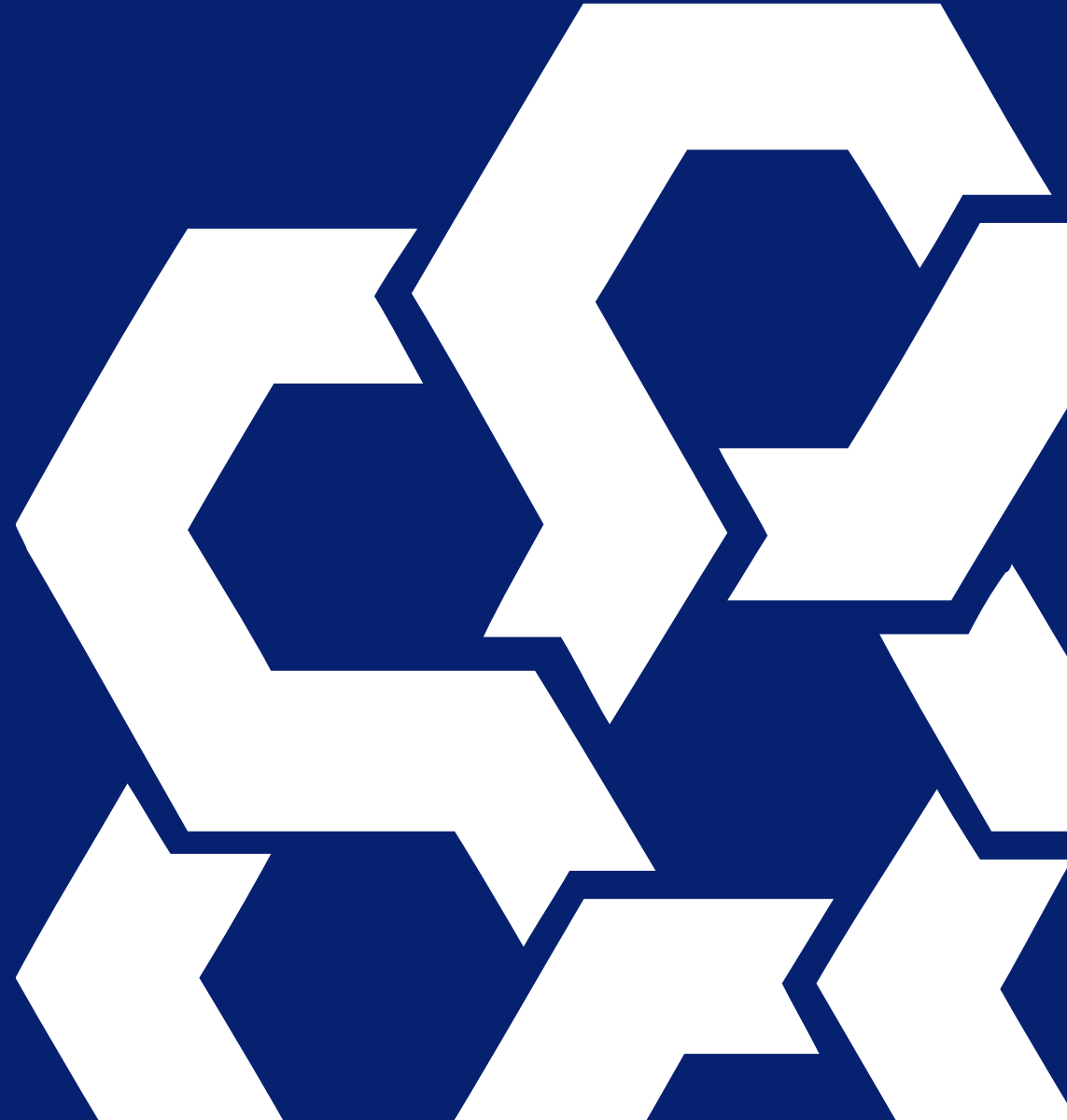
**1** Background

**2** Improving disclosures about business combinations

**3** The accounting for goodwill

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# Background



# Background



Objective

To improve the information entities provide to users of financial statements (users), at a reasonable cost, about the business combinations those entities make.



Path forward

The IASB redeliberated its preliminary views in the Discussion Paper, taking into account stakeholders' feedback on those preliminary views. The IASB will publish an exposure draft with revised proposals.



Project History



## The IASB's tentative decisions

	IASB's tentative decisions
Disclosures about business combinations	<ul style="list-style-type: none"> <li>• Disclose performance information about <b>strategic business combinations</b></li> <li>• <b>Exempt an entity from disclosing some information in specific circumstances</b></li> <li>• Identify information using an entity's <b>key management personnel (KMP)</b></li> <li>• Other improvements to existing disclosures, including disclosing quantitative information about expected synergies</li> </ul>
Accounting for goodwill	<ul style="list-style-type: none"> <li>• Retain the impairment-only model (no amortisation)</li> <li>• Simplify calculation of value in use</li> <li>• Retain requirement to perform impairment test annually</li> <li>• Clarifications on how an entity allocates goodwill to cash-generating units</li> </ul>

## A balanced package of proposals

### Overall package

- Balance between providing useful information while keeping costs at a reasonable level
- Help users more effectively assess management’s decision to acquire a business

Proposals	Considerations	
	Improve information at a reasonable cost	Reduce cost and complexity without reducing information
Disclose performance of business combinations	✓	
Improve existing disclosures (expected synergies, pro forma etc)	✓	
Improve impairment test effectiveness	✓	
Simplify value in use		✓

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## Improving disclosures about business combinations





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## Overall feedback

### Overall message

Many respondents, including almost all users, agreed with the preliminary views. However, many respondents, including almost all preparers, disagreed. Respondents identified costs associated with the preliminary views

### Summary of feedback

- Most preparers disagreed with the preliminary views because they expect the **costs of the disclosures to outweigh the benefits**:
  - **Monetary costs**: for example, costs of collecting and auditing the information; and
  - **Proprietary costs**: for example, from disclosing information some consider to be commercially sensitive and potential litigation
- Many respondents said information about the performance of business combinations should be provided in **management commentary rather than financial statements**

## Feedback

The management approach	Costs
<p><b>Feedback summary:</b></p> <ul style="list-style-type: none"> <li>• Most agreed the use of a management approach would help reduce cost of compliance. However, some said that the reduction in the costs is not sufficient</li> </ul> <p><b>Is the CODM the right level of management?</b></p> <ul style="list-style-type: none"> <li>• Mixed feedback:           <ul style="list-style-type: none"> <li>○ many said using CODM to identify business combinations is a practical approach</li> <li>○ many said using CODM may result in users not receiving all material information or too much information</li> <li>○ we observed confusion about the link between the preliminary views and segment reporting</li> </ul> </li> </ul>	<p><b>4 key contributors to cost:</b></p> <ul style="list-style-type: none"> <li>• <b>Commercial sensitivity</b>—disclosure could contain sensitive information that, if disclosed, could harm the entity</li> <li>• <b>Forward-looking</b>—disclosure could contain information about the future that, if disclosed, could increase litigation risk</li> <li>• <b>Integration</b>—entity might 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</li> <li>• <b>Auditability</b>—some information that would be required by the preliminary views might be costly, or difficult, to audit</li> </ul>

## IASB's response

Feedback	IASB's response
<ul style="list-style-type: none"> <li>Information belongs in management commentary</li> </ul>	<ul style="list-style-type: none"> <li>Reconfirmed its preliminary view that the information can be required in financial statements (slide 12)</li> </ul>
<ul style="list-style-type: none"> <li>Information could be commercially sensitive or forward-looking</li> </ul>	<ul style="list-style-type: none"> <li>Exempt an entity from disclosing some information in specific circumstances (slide 13)</li> </ul>
<ul style="list-style-type: none"> <li>Entities might be required to disclose too much information</li> </ul>	<ul style="list-style-type: none"> <li>Require disclosure of information for only strategic business combinations (slide 14)</li> </ul>
<ul style="list-style-type: none"> <li>Concerns regarding the use of CODM to identify information to be disclosed</li> </ul>	<ul style="list-style-type: none"> <li>Require disclosure of information reviewed by KMP (slide 16)</li> </ul>
<ul style="list-style-type: none"> <li>Expected synergies can be hard to quantify and not comparable if not defined</li> </ul>	<ul style="list-style-type: none"> <li>Clarify preliminary views about expected synergies (slide 18)</li> </ul>

## Location of information

Feedback	IASB's observations and decisions
<ul style="list-style-type: none"> <li>The information does not conceptually belong in financial statements</li> </ul>	<ul style="list-style-type: none"> <li>The information can be required in financial statements because it relates to the items recognised in the financial statements</li> </ul>
<ul style="list-style-type: none"> <li>The information could be forward-looking</li> <li>Disclosing such information could expose an entity to litigation risks</li> </ul>	<ul style="list-style-type: none"> <li>Some consider the information not to be forward-looking because it is information about assumptions underpinning a past transaction, not possible future events or transactions</li> <li>Even if the information is forward-looking, some say it meets the conditions in paragraph 3.6 of the <i>Conceptual Framework for Financial Reporting</i> for inclusion in financial statements</li> </ul>

## Exemption

Preliminary view	Amended proposal
No exemption	An entity may be exempted from disclosing some information <b>if doing so can be expected to prejudice seriously an entity’s objective for a business combination</b>

### Application guidance

The IASB will accompany the exemption with application guidance, which will include:

- Requirements—for example disclosing the reason for applying the exemption for each item of information
- Considerations of when it is appropriate to use the exemption—for example, it would be inappropriate if that information was already disclosed elsewhere

### Rationale

- Address concerns regarding harm that may be caused by commercial sensitivity that might arise from a range of sources—for example, competitors using the information
- Address some elements of concerns regarding litigation risk—for example, if the risk arises because an entity failed to meet an objective as a result of the disclosure

## Strategic business combinations

Preliminary view	Amended proposal
Require an entity to disclose information about the performance of business combinations that are monitored by an entity's <b>CODM</b>	Require an entity to disclose information about the performance of business combinations that are <b>strategic</b>
Thresholds	
<b>Quantitative thresholds</b> —Revenue, operating profit or assets of acquired business constitutes at least 10% of the acquirer's comparative amounts	<b>Qualitative thresholds</b> —business combination results in entity entering a new geographical location or a new major line of business
Rationale	
<ul style="list-style-type: none"> <li>• Users will receive information about the most important business combinations</li> <li>• Focusing on a subset of business combinations helps to reduce the cost of disclosing the information</li> <li>• More targeted identification of business combinations compared to the IASB's preliminary view</li> </ul>	

## Summary of key disclosure decisions

	<b>All material business combinations</b>	<b>Only ‘strategic’ business combinations</b>
<b>Proposed exemption applies</b>	In year of acquisition, quantitative information about expected synergies	In year of acquisition, information about management’s objectives and targets  Subsequently, a qualitative statement of whether actual performance met the entity’s objective and target
<b>No proposed exemption</b>	In year of acquisition, strategic rationale for undertaking the business combination	Actual performance in subsequent periods

## Identifying information to be disclosed

Preliminary view	Amended proposal
Require an entity to disclose information about the performance of a business combination based on information monitored by the entity's <b>CODM</b>	Require an entity to disclose information based on what is reviewed by the <b>key management personnel</b> <sup>1</sup> , as defined in IAS 24 <i>Related Party Disclosures</i>

Rationale
<ul style="list-style-type: none"> <li>• Retains benefits of CODM approach:               <ul style="list-style-type: none"> <li>○ Focuses on information provided to senior management. This is most likely to be information relevant to users; and</li> <li>○ Uses an existing term</li> </ul> </li> <li>• Avoids drawbacks of CODM approach:               <ul style="list-style-type: none"> <li>○ Not associated with segment reporting; and</li> <li>○ More adaptive to entities with different reporting structures</li> </ul> </li> </ul>

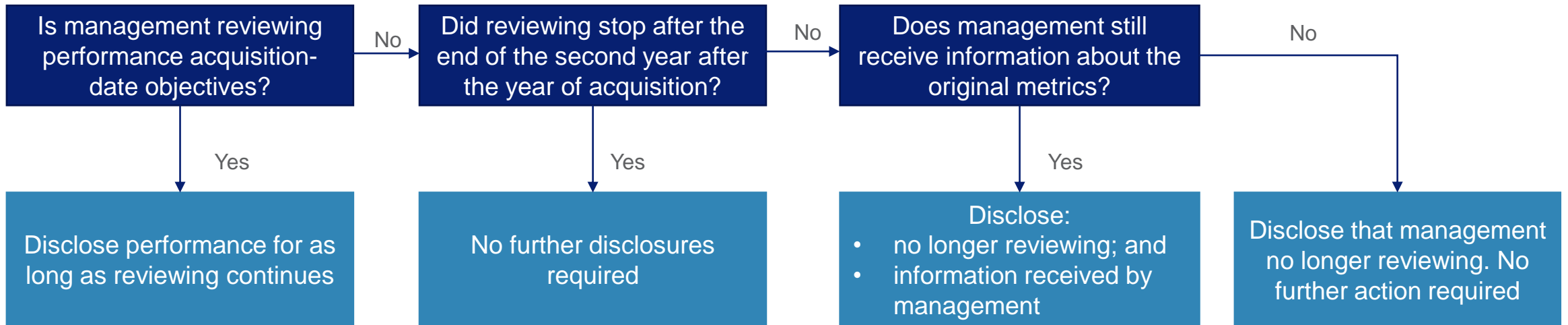
<sup>1</sup> KMP are persons having authority and responsibility for planning, directing and controlling the activities of the entity, directly or indirectly, including any director of that entity



## Duration of disclosure

In considering how long an entity should be required to disclose information about the performance of its strategic business combinations, the IASB seeks to achieve a balance between:

- Ensuring users receive information about a business combination for a reasonable amount of time; and
- Preparers not being required to disclose the information indefinitely



## Expected synergies

### Preliminary view

Require an entity to disclose quantitative information about synergies expected from a business combination

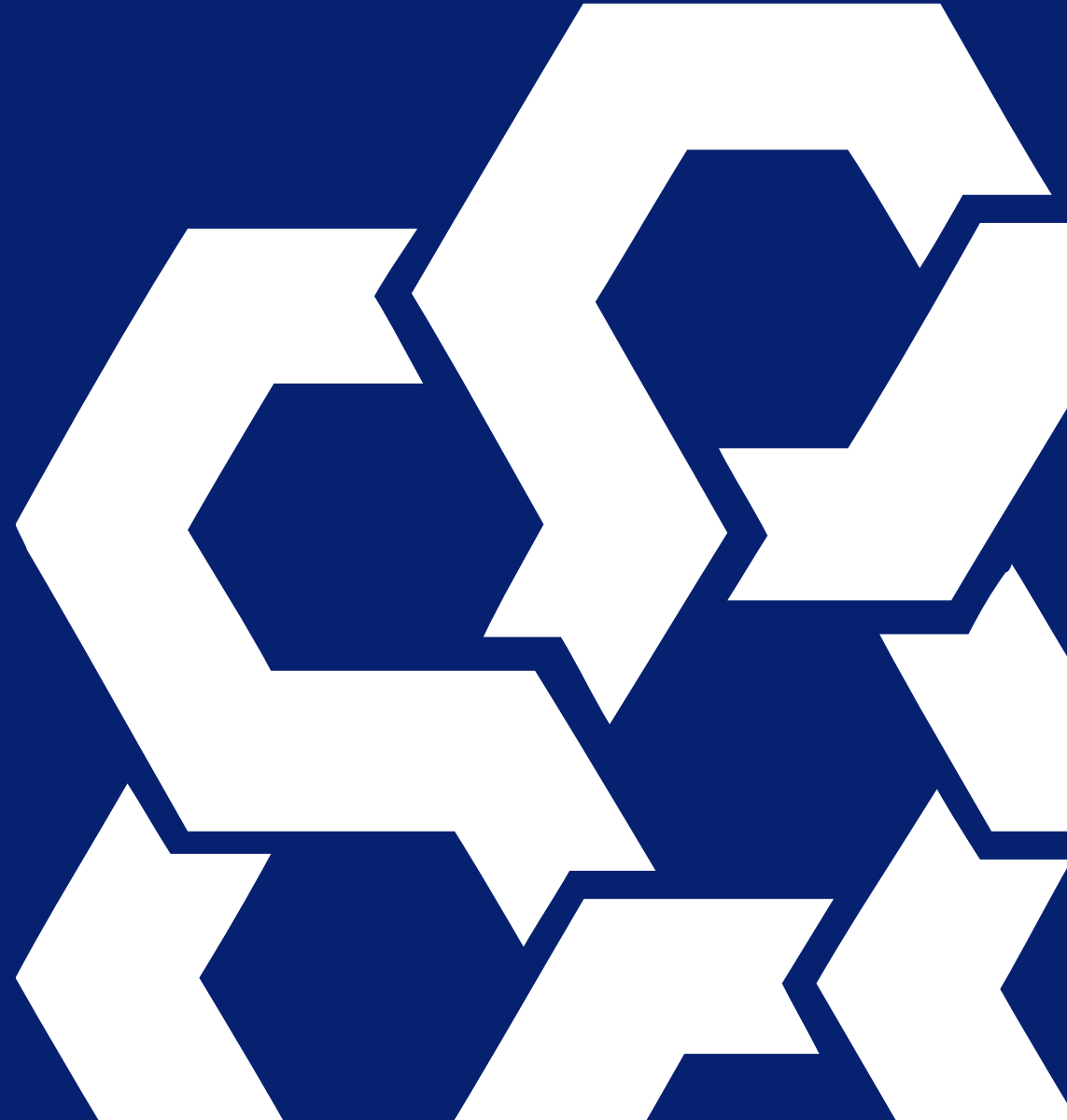
IASB's proposal	Rationale
<ul style="list-style-type: none"> <li>Require an entity disclose quantitative information about expected synergies</li> </ul>	<ul style="list-style-type: none"> <li>Academic evidence and feedback suggest that the information is useful and many entities are already providing the information</li> <li>Concerns from preparers about commercial sensitivity are dealt with by proposing an exemption in specific circumstances (see slide 13)</li> </ul>
<ul style="list-style-type: none"> <li>Information to be required in year of acquisition only</li> </ul>	<ul style="list-style-type: none"> <li>Feedback from stakeholder suggests it might be difficult for an entity to follow up on the achievement of synergies</li> </ul>
<ul style="list-style-type: none"> <li>Not to define expected synergies</li> </ul>	<ul style="list-style-type: none"> <li>Review of information suggests there is a common understanding of 'synergies'</li> </ul>
<ul style="list-style-type: none"> <li>Allow an entity to disclose a range rather than precise amount</li> </ul>	<ul style="list-style-type: none"> <li>Entities often do not calculate the precise amount of expected synergies</li> </ul>

## Other frequently asked questions

Question	Response
<p><b>What if the acquired business is integrated with the existing business?</b></p>	<p>If integration is planned, the entity’s objectives, targets and metrics might be about the combined business rather than the acquired business in isolation</p> <p>An entity would not be required to directly attribute the performance of a combined business to pre-existing and acquired businesses</p>
<p><b>Would the information required by the IASB’s proposals be auditable?</b></p>	<p>Most auditors said the information would be auditable at additional cost. The IASB expects an auditor would be able to verify :</p> <ul style="list-style-type: none"> <li>• whether the information disclosed is information management receives to review the business combination; and</li> <li>• whether there is adequate explanation of how the information has been prepared</li> </ul>
<p><b>Why is the IASB requiring this information only for business combinations and not other types of transactions?</b></p>	<p>The project began in response to PIR of IFRS 3, where we heard users rely on information from impairment test to understand the success of a business combination</p> <p>Feedback from investors suggests business combinations are viewed as a riskier form of investment</p>

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# The accounting for goodwill



## Areas of focus

Area of focus	IASB proposals
<ul style="list-style-type: none"> <li>Whether amortisation of goodwill should be reintroduced</li> </ul>	<ul style="list-style-type: none"> <li>In November 2022 the IASB decided not to explore amortisation of goodwill further</li> </ul>
<ul style="list-style-type: none"> <li>Whether the cost and complexity of the impairment test of cash-generating units (CGUs) containing goodwill can be reduced</li> </ul>	<ul style="list-style-type: none"> <li>In March 2023 the IASB tentatively decided to propose changes to how value in use is estimated</li> <li>In May 2023 the IASB tentatively decided to retain the requirement to perform the quantitative impairment test annually</li> </ul>
<ul style="list-style-type: none"> <li>Whether the impairment test can be made more effective at recognising impairment losses on goodwill on a timelier basis</li> </ul>	<ul style="list-style-type: none"> <li>In July 2023 the IASB tentatively decided to:               <ul style="list-style-type: none"> <li>Clarify the requirements for how an entity allocates goodwill to CGUs; and</li> <li>Require an entity to disclose the reportable segments in which CGUs containing goodwill are included</li> </ul> </li> </ul>

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## Feedback and decision on amortisation

<b>Preliminary view</b>	<ul style="list-style-type: none"><li>• Retain the impairment-only approach (small majority)</li></ul>
<b>Feedback</b>	<ul style="list-style-type: none"><li>• Respondents' views remain mixed and <b>entrenched</b></li><li>• The arguments to support either approach are <b>often diametrically opposed</b> and <b>unlikely to be reconciled</b>. Many of the arguments provided had been made during the development of IFRS 3 or during the course of this project</li><li>• Important to maintain convergence with US GAAP</li></ul>
<b>Tentative decision</b>	<ul style="list-style-type: none"><li>• In November 2022, the IASB tentatively decided to retain the impairment-only approach</li><li>• The IASB concluded that extensive evidence collected did not demonstrate a compelling case for change</li></ul>

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## Feedback

### Reasons for reintroducing amortisation

#### Conceptual reasons

- Goodwill is a wasting asset and amortisation of goodwill would reflect its consumption
- Amortisation prevents the recognition of internally generated goodwill
- A reliable estimate of useful life can be made
- Amortisation helps hold management accountable

#### Practical reasons

- The impairment test is not working and this could be resolved by reintroducing amortisation
- Goodwill balances are too high
- Amortisation is simple and less costly
- Earnings would be less volatile

### Reasons for retaining impairment-only approach

#### Conceptual reasons

- Goodwill is not a wasting asset with a determinable useful life
- Impairment losses provide users with more useful information than amortisation
- The useful life of goodwill cannot be estimated reliably
- The impairment-only model helps hold management accountable better than an amortisation model

#### Practical reasons

- Reintroducing amortisation would not resolve concerns about the impairment test
- Compelling evidence for change has not been identified

## Feedback on cost and complexity

Preliminary view	Feedback
<ul style="list-style-type: none"> <li>• Remove the requirement to perform the quantitative impairment test annually</li> </ul>	<ul style="list-style-type: none"> <li>• Many disagreed</li> <li>• Respondents questioned extent of cost reduction and the effect on the effectiveness of the impairment test</li> </ul>
<ul style="list-style-type: none"> <li>• Simplify how an entity estimates value in use by:               <ul style="list-style-type: none"> <li>○ allowing an entity to discount post-tax cash flows with post-tax discount rates; and</li> <li>○ removing restriction from including cash flows arising from future restructuring</li> </ul> </li> </ul>	<ul style="list-style-type: none"> <li>• General support for simplifying value in use estimations</li> <li>• These simplifications will also help align accounting requirements with market practice</li> </ul>
	<ul style="list-style-type: none"> <li>• Some respondents view the IASB having potentially conflicting goals between simplifying the impairment test and improving its effectiveness</li> </ul>



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## Tentative decisions on cost and complexity

### Preliminary view

- Remove requirement to perform the quantitative impairment test annually

### Tentative decision

- In May 2023 the IASB decided to retain the requirement to perform the quantitative impairment test annually in IAS 36
- The IASB was persuaded by feedback on:
  - The potential loss of information disclosed to users;
  - The extent of any cost reduction that would result from the preliminary view; and
  - The effect on the effectiveness of the impairment test

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## Tentative decisions on cost and complexity

### Preliminary views

- Allow an entity to discount post-tax cash flows with post-tax discount rates
- Remove restriction from including cash flows from future restructuring

### Tentative decision

- In March 2023, the IASB tentatively decided to confirm preliminary views
- Propose to require use of internally consistent assumptions for cash flows and discount rates
- The IASB discussed a number of safeguards in IAS 36 *Impairment of Assets* that help in auditing and enforcing inclusion of cash flows from future restructuring (for example that the asset tested must be in its current condition)

## Feedback on impairment test effectiveness

Preliminary view	Feedback
<ul style="list-style-type: none"> <li>• The IASB identified two broad reasons for concerns about the possible delay in recognising impairment losses on goodwill:               <ul style="list-style-type: none"> <li>○ management over-optimism; and</li> <li>○ shielding</li> </ul> </li> </ul>	<ul style="list-style-type: none"> <li>• Most agreed</li> </ul>
<ul style="list-style-type: none"> <li>• Not feasible to design a different impairment test for CGUs containing goodwill that is significantly more effective at recognising impairment losses on goodwill on a timely basis than the impairment test in IAS 36 at a reasonable cost</li> </ul>	<ul style="list-style-type: none"> <li>• Most agreed</li> <li>• Some suggested different impairment tests (for example, the headroom approach)</li> <li>• Many suggested ways to improve the application and effectiveness of the test in IAS 36</li> <li>• A few said the purpose of the impairment test is misunderstood</li> </ul>

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## Reducing shielding

### Impairment test change

- Guidance on allocation goodwill to CGUs or groups of CGUs

### Tentative decision

- In July 2023 the IASB tentatively decided to propose a package of changes to the language used in IAS 36 designed to help entities allocate goodwill to CGUs or groups of CGUs on a more effective basis.
- Changes include:
  - Amending reference to ‘goodwill is monitored’
  - Clarifying that allocating goodwill no higher than an operating segment is a safeguard and not a default
  - Clarifying why an entity would allocate goodwill to a group of CGUs rather than individual CGUs

## Reducing management over-optimism

<b>Impairment test change</b>	<ul style="list-style-type: none"> <li>Disclosing in which reportable segment CGUs containing goodwill are included</li> </ul>		
<b>Tentative decision</b>	<ul style="list-style-type: none"> <li>Intended to help reduce management over-optimism</li> <li>Links the disclosure of assumptions used in the impairment test to segment information</li> </ul>		
<b>Example</b>	<b>Segment</b>	<b>CGU</b>	<b>Value of goodwill</b>
	A	CGU 1	CU175
		Group of CGUs X	CU300
	B	CGU 2	CU250

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