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(submitted via the IASB website)

27 June 2024

Dear Andreas,

AASB submission on IASB Exposure Draft/2024/1 Business Combinations – Disclosures, Goodwill and Impairment: Proposed amendments to IFRS 3 and IAS 36

The Australian Accounting Standards Board (AASB) welcomes the opportunity to provide comments on the International Accounting Standards Board (IASB) Exposure Draft 2024/1. In formulating these comments, the views of our Australian stakeholders were sought and considered. This included:

- consultation with the AASB's User Advisory Committee, comprising a range of primary users of financial statements;
- consultation with the AASB's Disclosure Initiative Advisory Panel, comprising subject matter experts across a range of stakeholder groups;
- targeted consultations with key stakeholders, such as professional bodies, auditors and preparers in Australia.

The AASB acknowledges the IASB's efforts and supports aspects of the proposals relating to IAS 36 *Impairment of Assets*. However, the AASB does not support the proposals relating to strategic business combinations and synergies. Users we spoke with failed to see sufficient value in these disclosures. Further, we consider that this information does not fall within the remit of financial reporting, noting that similar information is not required for other assets.

The AASB's specific concerns and recommendations in relation to the proposals are detailed in the Appendix. If you have any questions regarding this letter, please do not hesitate to contact me or Helena Simkova, Director (hsimkova@aasb.gov.au).

Yours sincerely,

Dr. Keith Kendall
Chair – AASB

APPENDIX

AASB responses to questions raised in the IASB Exposure Draft/2024/1 *Business Combinations—Disclosures, Goodwill and Impairment*: Proposed amendments to IFRS 3 and IAS 36

Question 1— Disclosures: Performance of a business combination (proposed paragraphs B67A–B67G of IFRS 3)
In the PIR of IFRS 3 and in responses to the DP the IASB heard that: • users need better information about business combinations to help them assess whether the price an entity paid for a business combination is reasonable and how the business combination performed after acquisition. In particular, users said they need information to help them assess the performance of a business combination against the targets the entity set at the time the business combination occurred (see paragraphs BC18–BC21). • preparers of financial statements are concerned about the cost of disclosing that information. In particular, preparers said the information would be so commercially sensitive that its disclosure in financial statements should not be required and disclosing this information could expose an entity to increased litigation risk (see paragraph BC22). Having considered this feedback, the IASB is proposing changes to the disclosure requirements in IFRS 3 that, in its view, appropriately balance the benefits and costs of requiring an entity to disclose this information. It therefore expects that the proposed disclosure requirements would provide users with more useful information about the performance of a business combination at a reasonable cost. In particular, the IASB is proposing to require an entity to disclose information about the entity's acquisition-date key objectives and related targets for a business combination and whether these key objectives and related targets are being met (information about the performance of a business combination). The IASB has responded to preparers' concerns about disclosing that information by proposing: • to require this information for only a subset of an entity's business combinations— strategic business combinations (see question 2); and • to exempt entities from disclosing some items of this information in specific circumstances (see question 3). (a) Do you agree with the IASB's proposal to require an entity to disclose information about the performance of a strategic business combination, subject to an exemption? Why or why not? In responding, please consider whether the proposals appropriately balance the benefits of requiring an entity to disclose the information with the costs of doing so. (b) If you disagree with the proposal, what specific changes would you suggest to provide users with more useful information about the performance of a business combination at a reasonable cost?

The AASB has fundamental concerns about the proposals to require disclosure of information about the acquisition-date key objectives, related targets and subsequent performance of a strategic business combination. In its response to DP/2020/1, the AASB expressed concerns regarding the auditability and location of the proposed disclosures. The AASB considers that these concerns were not sufficiently addressed in the ED and, therefore, the AASB continues to consider that this information does not fall within the remit of financial reporting. Specifically, the AASB notes:

- These disclosures may better fit in management commentary rather than in the financial statements, given that the aim of management commentary is to provide primary users of financial reports with information that is useful in assessing management's stewardship of the entity's economic resources.
- Similar information is not required for other assets (e.g. purchase of new inventory or new property, plant and equipment, or investment in intangible assets, to initiate a new revenue stream), even though users would have a similar interest in the success, or not, of such projects.

- Users failed to see value in the proposed disclosures, noting that they would expect vague or boilerplate disclosures which are unlikely to provide useful information.
- Stakeholders raised concerns about the auditability (and associated cost) of the proposed disclosures. For example:
  - It would be difficult, and costly, to provide assurance that attributes an improvement in performance to the acquisition and not to other factors in the rest of the business when integration has occurred, and the acquisition-date targets are based on the integrated operations.
  - There is a difference between the auditor opining that acquisition-date objectives and targets faithfully represent management's view, versus the objective and target being a true and fair view. This could contribute to the user expectation gap of what an audit does or does not cover.

Question 2— Disclosures: Strategic business combinations (proposed paragraph B67C of IFRS 3)
The IASB is proposing to require an entity to disclose information about the performance of a business combination (that is, information about the entity's acquisition-date key objectives and related targets for the business combination and whether these key objectives and related targets are being met) for only strategic business combinations—a subset of material business combinations. A strategic business combination would be one for which failure to meet any one of an entity's acquisition-date key objectives would put the entity at serious risk of failing to achieve its overall business strategy. The IASB is proposing that entities identify a strategic business combination using a set of thresholds in IFRS 3—a business combination that met any one of these thresholds would be considered a strategic business combination (threshold approach) (see paragraphs BC56–BC73). The IASB based its proposed thresholds on other requirements in IFRS Accounting Standards and the thresholds regulators use to identify particularly important transactions for which an entity is required to take additional steps such as providing more information or holding a shareholder vote. The proposed thresholds are both quantitative (see paragraphs BC63–BC67) and qualitative (see paragraphs BC68–BC70). (a) Do you agree with the proposal to use a threshold approach? Why or why not? If you disagree with the proposal, what approach would you suggest and why? (b) If you agree with the proposal to use a threshold approach, do you agree with the proposed thresholds? Why or why not? If not, what thresholds would you suggest and why?

The AASB does not support the proposal to require additional disclosures about strategic business combinations. There is already an existing threshold (materiality) that is applied when assessing disclosure of information. Thus, no additional thresholds should be introduced.

In addition to our comments above, we consider that a closed-list approach using a specific set of thresholds may capture "un-strategic" acquisitions (i.e. not the population of acquisitions intended by the IASB), further highlighting the challenges of these proposals.

- The quantitative thresholds are too low. For example;
  - It may be excessively easy to meet one of the thresholds based on the nature of the business (for example, service businesses and the asset threshold).
  - The thresholds will result in comparing the acquired business at fair value, including goodwill, against the acquirer's business which may have assets recorded at historical cost.
- The qualitative thresholds will be subject to interpretation, may be challenging to apply, and may not capture the appropriate business combinations. For example;
  - It is unclear whether the term 'major' relates to both the thresholds i.e. 'lines of business' and 'geographies', or just the former.
  - A small acquisition in a new geography may be testing the market, rather than being strategic.

Question 3— Disclosures: Exemption from disclosing information (proposed paragraphs B67D–B67G of IFRS 3)
The IASB is proposing to exempt an entity from disclosing some of the information that would be required applying the proposals in this ED in specific circumstances. The exemption is designed to respond to preparers' concerns about commercial sensitivity and litigation risk but is also designed to be enforceable and auditable so that it is applied only in the appropriate circumstances (see paragraphs BC74–BC107). The IASB proposes that, as a principle, an entity be exempt from disclosing some information if doing so can be expected to prejudice seriously the achievement of any of the entity's acquisition-date key objectives for the business combination (see paragraphs BC79–BC89). The IASB has also proposed application guidance (see paragraphs BC90–BC107) to help entities, auditors and regulators identify the circumstances in which an entity can apply the exemption. (a) Do you think the proposed exemption can be applied in the appropriate circumstances? If not, please explain why not and suggest how the IASB could amend the proposed principle or application guidance to better address these concerns. (b) Do you think the proposed application guidance would help restrict the application of the exemption to only the appropriate circumstances? If not, please explain what application guidance you would suggest to achieve that aim.

The nature of the proposed disclosures gives rise to a greater than normal risk of commercially sensitive information being required to be disclosed, further highlighting our concerns with the proposals. Further, the AASB considers that the exemption does not sufficiently address the matter of commercial sensitivity as it has been defined too narrowly. For example, because the exemption is designed to apply only to the disclosure of information that can be expected to prejudice seriously the achievement of any of the acquirer's acquisition-date key objectives for the business combination rather than prejudicing seriously the entity as a whole, makes it too limited. A preparer noted that disclosure of a hurdle rate[1] could seriously prejudice future acquisitions because a competitor could use that information to outbid the entity in future deals. Those future deals are unlikely to relate to the acquisition-date key objectives for the current business combination, and thus the exemption would not apply.

[1] A hurdle rate, also known as a minimum acceptable rate of return (MARR), is the lowest rate of return managers or investors expect to receive on an investment or a project.

Question 4— Disclosures: Identifying information to be disclosed (proposed paragraphs B67A–B67B of IFRS 3)
The IASB is proposing to require an entity to disclose information about the performance of the entity's strategic business combinations (that is, information about its acquisition-date key objectives and related targets for a strategic business combination and whether these key objectives and related targets are being met) that is reviewed by its key management personnel (see paragraphs BC110–BC114). The IASB's proposals would require an entity to disclose this information for as long as the entity's key management personnel review the performance of the business combination (see paragraphs BC115–BC120). The IASB is also proposing (see paragraphs BC121–BC130) that if an entity's key management personnel: • do not start reviewing, and do not plan to review, whether an acquisition-date key objective and the related targets for a business combination are met, the entity would be required to disclose that fact and the reasons for not doing so; • stop reviewing whether an acquisition-date key objective and the related targets for a business combination are met before the end of the second annual reporting period after the year of acquisition, the entity would be required to disclose that fact and the reasons it stopped doing so; and • have stopped reviewing whether an acquisition-date key objective and the related targets for a business combination are met but still receive information about the metric that was originally used to measure the achievement of that key objective and the related targets, the entity would be required to disclose information about the metric during the period up to the end of the second annual reporting period after the year of acquisition. (a) Do you agree that the information an entity should be required to disclose should be the information reviewed by the entity's key management personnel? Why or why not? If not, how do you suggest an entity be required to identify the information to be disclosed about the performance of a strategic business combination? (b) Do you agree that: (i) an entity should be required to disclose information about the performance of a business combination for as long as the entity's key management personnel review that information? Why or why not? (ii) an entity should be required to disclose the information specified by the proposals when the entity's key management personnel do not start or stop reviewing the achievement of a key objective and the related targets for a strategic business combination within a particular time period? Why or why not?

The AASB does not support the proposal that an entity should be required to disclose information about the performance of the entity's strategic business combinations. In addition to our concerns expressed earlier, we heard concerns from our stakeholders that the way in which these particular requirements have been written is confusing, especially with regards to what is required when an entity's key management personnel do not start or stop reviewing within the specified time period.

Question 5— Disclosures: Other proposals
The IASB is proposing other amendments to the disclosure requirements in IFRS 3. These proposals relate to: *New disclosure objectives (proposed paragraph 62A of IFRS 3)* The IASB proposes to add new disclosure objectives in proposed paragraph 62A of IFRS 3 (see paragraphs BC23–BC28). *Requirements to disclose quantitative information about expected synergies in the year of acquisition (proposed paragraph B64(ea) of IFRS 3)* The IASB proposes: • to require an entity to describe expected synergies by category (for example, revenue synergies, cost synergies and each other type of synergy); • to require an entity to disclose for each category of synergies: • the estimated amounts or range of amounts of the expected synergies; • the estimated costs or range of costs to achieve these synergies; and • the time from which the benefits expected from the synergies are expected to start and how long they will last; and • to exempt an entity from disclosing that information in specific circumstances. See paragraphs BC148–BC163. The strategic rationale for a business combination (paragraph B64(d) of IFRS 3) The IASB proposes to replace the requirement in paragraph B64(d) of IFRS 3 to disclose the primary reasons for a business combination with a requirement to disclose the strategic rationale for the business combination (see paragraphs BC164–BC165). *Contribution of the acquired business (paragraph B64(q) of IFRS 3)* The IASB proposes to amend paragraph B64(q) of IFRS 3 to improve the information users receive about the contribution of the acquired business (see paragraphs BC166–BC177). In particular, the IASB proposes: • to specify that the amount of profit or loss referred to in that paragraph is the amount of operating profit or loss (operating profit or loss will be defined as part of the IASB's Primary Financial Statements project); • to explain the purpose of the requirement but add no specific application guidance; and • to specify that the basis for preparing this information is an accounting policy. *Classes of assets acquired and liabilities assumed (paragraph B64(i) of IFRS 3)* The IASB proposes to improve the information entities disclose about the pension and financing liabilities assumed in a business combination by deleting the word 'major' from paragraph B64(i) of IFRS 3 and adding pension and financing liabilities to the illustrative example in paragraph IE72 of the Illustrative Examples accompanying IFRS 3 (see paragraphs BC178–BC181). *Deleting disclosure requirements (paragraphs B64(h), B67(d)(iii) and B67(e) of IFRS 3)* The IASB proposes to delete some disclosure requirements from IFRS 3 (see paragraphs BC182–BC183). Do you agree with the proposals? Why or why not?

The AASB does not support the proposal to disclose synergies for material acquisitions. We have concerns about auditability, within reasonable costs, of the proposed synergy disclosures, as quantifying expected synergies will be highly judgmental. Further, users noted that they would not see value in these disclosures, particularly because they would not rely on any future reporting of realised synergies. Therefore, the costs of preparing the required information would exceed the expected benefits to users of financial statements.

Question 6— Changes to the impairment test (paragraphs 80–81, 83, 85 and 134(a) of IAS 36)
During the PIR of IFRS 3, the IASB heard concerns that the impairment test of cash generating units containing goodwill results in impairment losses sometimes being recognised too late. Two of the reasons the IASB identified (see paragraphs BC188–BC189) for these concerns were: • shielding; and • management over-optimism. The IASB is proposing amendments to IAS 36 that could mitigate these reasons (see paragraphs BC192–BC193). *Proposals to reduce shielding* The IASB considered developing a different impairment test that would be significantly more effective at a reasonable cost but concluded that doing so would not be feasible (see paragraphs BC190–BC191). Instead, the IASB is proposing changes to the impairment test (see paragraphs 80–81, 83 and 85 of IAS 36) to reduce shielding by clarifying how to allocate goodwill to cash generating units (see paragraphs BC194–BC201). *Proposal to reduce management over-optimism* The IASB's view is that management over-optimism is, in part, better dealt with by enforcers and auditors than by amending IAS 36. Nonetheless, the IASB is proposing to amend IAS 36 to require an entity to disclose in which reportable segment a cash generating unit or group of cash-generating units containing goodwill is included (see paragraph 134(a) of IAS 36). The IASB expects this information to provide users with better information about the assumptions used in the impairment test and therefore allow users to better assess whether an entity's assumptions are over-optimistic (see paragraph BC202). (a) Do you agree with the proposals to reduce shielding? Why or why not? (b) Do you agree with the proposal to reduce management over-optimism? Why or why not?

The AASB agrees with the proposed clarification on goodwill allocation to reduce shielding and with the additional disclosure to reduce the impact of management over-optimism. To further reduce shielding, we also suggest that the IASB requires an entity to disclose the method used to allocate corporate costs, including disclosing the level to which the corporate costs were allocated.

Question 7— Changes to the impairment test: Value in use (paragraphs 33, 44–51, 55, 130(g), 134(d)(v) and A20 of IAS 36)
The IASB is proposing to amend how an entity calculates an asset's value in use. In particular, the IASB proposes: • to remove a constraint on cash flows used to calculate value in use. An entity would no longer be prohibited from including cash flows arising from a future restructuring to which the entity is not yet committed or cash flows arising from improving or enhancing an asset's performance (see paragraphs BC204–BC214). • to remove the requirement to use pre-tax cash flows and pre-tax discount rates in calculating value in use. Instead, an entity would be required to use internally consistent assumptions for cash flows and discount rates (see paragraphs BC215–BC222). (a) Do you agree with the proposal to remove the constraint on including cash flows arising from a future restructuring to which the entity is not yet committed or from improving or enhancing an asset's performance? Why or why not? (b) Do you agree with the proposal to remove the requirement to use pre-tax cash flows and pre-tax discount rates in calculating value in use? Why or why not?

The AASB supports the proposed changes to the impairment test, with recommendations on clarification points as follows:

- The feedback we received indicated that the requirement for the cash flows to be derived from an asset in its current condition may not be clear. Whilst we acknowledge that paragraph 44A provides some guidance on the future cash flows of an asset in its current condition, we noted that some IASB members disagreed as in their view, these cash flows do not represent cash flows from an asset in its current condition (BC214). This implies a need for further clarification and guidance. This guidance could be provided in illustrative examples (IEs). We suggest replacing IE5 and IE6 with updated guidance rather than removing them completely.
- As the proposed changes to the value in use model bring it closer to the fair value model, we suggest that the IASB explains the difference between these two models in the Basis for Conclusions. A deeper understanding of these models could help preparers apply the requirements.

Question 8— Proposed amendments to IFRS X Subsidiaries without Public Accountability: Disclosures
The IASB proposes to amend the forthcoming IFRS X *Subsidiaries without Public Accountability: Disclosures* (Subsidiaries Standard) to require eligible subsidiaries applying the Subsidiaries Standard to disclose: •information about the strategic rationale for a business combination (proposed paragraph 36(ca) of the Subsidiaries Standard); •quantitative information about expected synergies, subject to an exemption in specific circumstances (proposed paragraphs 36(da) and 36A of the Subsidiaries Standard); •information about the contribution of the acquired business (proposed paragraph 36(j) of the Subsidiaries Standard); and •information about whether the discount rate used in calculating value in use is pretax or post-tax (paragraph 193 of the Subsidiaries Standard). See paragraphs BC252–BC256. Do you agree with the proposals? Why or why not?

Stakeholders indicated that the proposed disclosure requirements would be excessive for subsidiaries without public accountability and would result in increased costs to preparers without a comparative increase in benefits. We note that in Australia, a domestic disclosure standard is used by entities without public accountability. This standard does not include similar disclosure requirements. The AASB has not heard any concerns that the current disclosures are not sufficient for the users of those financial statements.

Question 9—Transition (proposed paragraph 64R of IFRS 3, proposed paragraph 140O of IAS 36 and proposed paragraph B2 of the Subsidiaries Standard)
The IASB is proposing to require an entity to apply the amendments to IFRS 3, IAS 36 and the Subsidiaries Standard prospectively from the effective date without restating comparative information. The IASB is proposing no specific relief for first-time adopters. See paragraphs BC257–BC263. Do you agree with the proposals? Why or why not? If you disagree with the proposals, please explain what you would suggest instead and why.

The AASB supports the proposal to implement the changes to the value in use model and the guidance on goodwill allocation prospectively without restating comparative information.