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Submitted to: www.ifrs.org

Dear Andreas

ED/2024/1 *Business Combinations – Disclosures, Goodwill and Impairment*

Thank you for the opportunity to comment on the Exposure Draft ED/2024/1 *Business Combinations – Disclosure, Goodwill and Impairment* (the ED). We acknowledge the importance and relevance of the topics discussed in the ED and appreciate the IASB's efforts to address feedback from previous consultation on these topics. The ED has been exposed for comment in New Zealand and some New Zealand constituents may comment directly to you.

Based on the feedback obtained from our New Zealand stakeholders, through a range of outreach and consultations, the NZASB does not support the proposed disclosure requirements relating to the performance targets and actual performance of strategic business combinations and expected synergies. Disclosing such information within the financial statements is not consistent with the type of information generally included within general-purpose financial reporting and bears a closer resemblance to management discussion and analysis (i.e. management commentary). The benefits of reporting this information are, at best, marginal. While the inclusion of this information in the financial statements may satisfy some investors' needs, it fails to address the fundamental issues associated with the accounting challenges relating to goodwill.

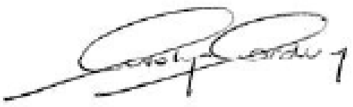
The NZASB have significant reservations about the commercial sensitivity of the proposed disclosure requirements and the consequential costs expected to be incurred to report on these required disclosures. Other forms of investment or major transactions such as capital investment, investment in internally generated intangibles, restructuring or significant disposals do not require similar level of disclosures, and these types of transactions can be as critical to an entity's success in achieving its overall business strategy. Considering the absence of disclosure requirements for investments in organic growth, the proposed additional disclosures on acquisitions would further widen the gap in financial reporting between these two different growth strategies. With the commercial sensitivity of the proposed requirements, this imbalance in financial reporting is reaching a critical juncture, potentially swaying strategic decision-making regarding these approaches.

Our recommendations and responses to the specific questions for respondents are set out in the Appendix to this letter.

We would like to take this opportunity to thank IASB member Ann Tarca and IASB staff members Vikash Kalidas, Rich Brown and Dehao Fang for their assistance with education and outreach events with the NZASB and New Zealand constituents.

If you have any queries or require clarification of any matters in this letter, please contact Alex Stainer (alex.stainer@xrb.govt.nz) or me.

Yours sincerely



Carolyn Cordery
Chair – New Zealand Accounting Standards Board

Appendix:

Question 1

In the PIR of IFRS 3 and in responses to the Discussion Paper 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?

Response to Question 1(a)

NZASB disagrees with introducing these proposals

1. The NZASB has significant concerns about the proposals relating to strategic business combinations. These concerns are similar to those that we raised in our comment letter on the IASB's 2020 Discussion Paper Business Combinations - Disclosures, Goodwill and Impairment, with respect to the disclosures proposed in that DP. While the IASB decreased the scope of the proposed disclosure requirements to focus only on strategic acquisitions, most of the concerns that we raised in our comment letter on the DP still stand with respect to the disclosures proposed in the ED. We recommend that the IASB does not move forward with these proposals for the reasons set out below.

Proposed disclosures not consistent with general purpose financial reporting

2. The NZASB consider that the proposed disclosures, particularly those related to management's targets and actual performance, are better suited to the management commentary or other forms of reporting outside the financial statements. It is not the role of general-purpose financial reporting to report on internal performance targets and dissect in detail performance targets for individual transactions, nor should it be its role to justify management’s specific decisions. General-purpose financial reporting should only include information that impartially reports the financial performance and position and provides explanations of relevant items in the financial statements. The NZASB does not consider that the proposed disclosures on performance targets and actual performance of acquisition are consistent with the principles of general-purpose financial reporting. These disclosures do not seem to relate to a specific item in the financial statements (other than indirectly to goodwill and its impairment).
3. By contrast, these disclosures seem to fit with the key elements of management commentary as per the IASB’s current Practice Statement *Management Commentary*, which include information that helps users understand “management’s objectives and its strategies for meeting those objectives” and “the critical performance measures and indicators that management uses to evaluate the entity’s performance against stated objectives”. The disclosures are also consistent with the proposal in the IASB’s recent ED *Management Commentary* that management commentary should aim to provide users with information that is useful in assessing management’s stewardship of the entity’s economic resources.
4. Using management commentary or other voluntary reporting provides greater flexibility for management to communicate its strategic objectives and progress against those objectives, without the constraints and assurance implications of including the information in the audited financial statements.

Disagree on the basis disclosures are commercially sensitive

5. Of concern to New Zealand stakeholders is the release of commercially sensitive information as part of these disclosures. The IASB acknowledges in its Basis for Conclusions that the majority of preparers noted that *'some of the information described in the preliminary views would be so commercially sensitive that its disclosure in financial statements should not be required'*. The IASB then brought together groups of both preparers and users to explore solutions that balance need for information and respond to some preparer concerns. The IASB then concluded that an exemption would respond to some concerns about commercial sensitivity.

6. The NZASB and its New Zealand stakeholders do not think the proposed exemption resolves the issue of commercial sensitivity inherent within the proposed disclosures. New Zealand organisations anticipate a competitive disadvantage as a result of the proposals, fearing competitors can use this information to undermine the company's strategy. The proposed disclosures bring a level of sensitivity that surpasses other commercially sensitive information reported in the financial statements; exposing the entity to additional scrutiny on critical strategic positions reflected in its performance targets and objectives. The consequences of this could be unpredictable and lead to operational disadvantages or risks they would not otherwise have been subject to. While investors may request such information, they may not have fully realised that it comes with a real performance cost to the entity and will by extension impact their investments.

7. In some cases, the risks arising from disclosing commercially sensitive information may even undermine the purpose behind the business combination and sway acquisition decisions to alternatives that do not require these disclosures.

8. The introduction of the exemption does not ease these concerns. It comes with its own additional costs and subjectivity. Even when an entity applies the exemption, it will create additional external scrutiny as to why it has not disclosed certain information, and potentially compromise the performance and operations of the entity moving forward regardless.

Does not fully address the underlying issue: goodwill impairment

9. Investors' demands for better information about business combinations stems from the persistent challenge in understanding and assessing the appropriateness of goodwill balances. These proposals fall short of addressing these fundamental concerns and only address an aspect of it. Investors are needing more than just performance metrics for acquisitions; they seek information that the goodwill balance faithfully reflects future economic benefits and that any impairment is recognised on a timely basis.

Further imbalance with disclosures for organic growth

10. These proposals exacerbate the existing disparity in disclosure obligations between investments made through acquisitions and those directed towards organic growth. Unlike acquisitions, other significant financial activities—such as capital investments,

development of internally generated intangibles, or organisational restructuring—do not mandate disclosures that correlate the expenditure with performance outcomes. Furthermore, there is no requirement for management to explicitly rationalise their investment or restructuring choices. Should these proposals be adopted, the resulting imbalance could significantly sway internal decision-making processes related to growth strategies, particularly in light of the critical issues surrounding the confidentiality of such disclosures.

Benefits outweighed by costs

11. Our consultations indicate a limited demand for this information among users. We expect that the benefits of the proposed disclosures will also be short-lived. There is a high marginal cost to preparing these disclosures, including costs relating to commercial sensitivity, as well as increased audit costs, particularly considering the subjective nature of the disclosure requirements. These costs seem disproportionate to the expected benefit.

12. In many jurisdictions there will already be similar forms of this information available to investors, including through, investor calls, ongoing disclosure requirements in capital markets and approvals for significant transactions. Material acquisitions in some circumstances may even be captured by the disclosures required for segment reporting. This type of information is often able to be gathered through other sources in a more timely and relevant manner without the required costs or inconsistency with general-purpose financial reporting principles.

Question 2

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?

Response to Question 2(a)

13. As noted in our response to Question 1, the NZASB does not support the proposals relating to strategic business combinations. Nevertheless, in case the IASB proceeds with the requiring proposed disclosures, we have responded to this question as we have several comments for the IASB to consider:

    (a) The label 'strategic business combinations' is misleading. All acquisitions could be considered strategic and using this label does not articulate well why these disclosures are necessary for certain acquisitions and not for others.

    (b) The quantitative thresholds do not reflect the label of 'strategic business combinations' and are too low to be consistent with the description of a 'strategic business combination' contained in ED's Basis for Conclusions in BC 54 and 55 (noted below). Additional guidance on how the qualitative thresholds reflect this description would also be beneficial.

BC 54

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.

BC55

In the IASB's view, strategic business combinations would capture business combinations of significant strategic value to an entity. An entity's overall business strategy could be put at serious risk if, for example, the entity:

(a) committed a large amount of capital to a business combination that subsequently failed to meet the entity's expectations; or

(b) failed to enter major new lines of business or geographies that are essential to the entity's overall business strategy through the business combination.

(c) Using a principled approach (with indicators instead of thresholds) would better support the basis for these disclosures and ensure the additional costs of these disclosures only apply to those acquisitions that merit it (based on the principle in paragraphs BC54 and BC55). The limitations involved with a threshold approach will add cost where the disclosures apply to those acquisitions not intended to be reported on or that do not warrant enhanced disclosure from a user perspective. Our rationale for using a principle-based approach is that it will:

(i) clarify the intention behind which acquisitions should be captured and why;
(ii) ensure that the additional costs of these disclosures will only apply to those acquisitions that merit reporting them;
(iii) help entities understand whether it is likely the principle will apply;
(iv) prevent 'close-calls' and incentives to game the proposed thresholds;
(v) help with the quality of disclosures and justify additional costs when required.

Question 3

The IASB is proposing to exempt an entity from disclosing some of the information that would be required applying the proposals in this Exposure Draft 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.

Response to Question 3(a) and (b)

14. As noted in Question 1, commercial sensitivity was a major concern expressed by constituents during our outreach activities – particularly in the context of New Zealand's relatively small economy. Even with the proposed exemption, the NZASB does not support the proposals for 'strategic business combinations' given the disclosures will require the release of commercially sensitive information. We do not consider that there can be an exemption that can address this particular concern while continuing to allow disclosures that achieve the proposed objectives in the ED.

15. The exemption as proposed is 'narrow' and accordingly will not prevent significant costs arising from disclosure of commercially sensitive information. The impacts on organisations from the disclosure of commercially sensitive information is not easily identifiable but will result in a real cost on the performance of the acquisition or wider reporting entity. With the introduction of these proposals, these impacts are likely to be widespread.

16. Application of the exemption in the proposed circumstances will be subjective and will therefore require negotiation between auditors and management. We expect that this will increase costs and increase the potential for diversity in practice. Organisations applying the exemption will also be subjected to additional scrutiny based on information not disclosed.

17. Entities that apply the exemption would not be required to report on the acquisition's key objectives and targets in the year of acquisition, but they would still be required to report on the actual performance for the year as per proposed paragraph B67A(b)(i) of IFRS 3. Information provided for actual performance is likely to be commercially sensitive. The application guidance does not make it clear how or why an entity should disclose actual performance without prejudicing the ongoing achievement of their objectives.

18. If the IASB proceeds with these proposals, then we recommend the following with respect to the application guidance:

    (a) to help restrict the use of the exemption to only the appropriate circumstances and ease costs of implementation and diversity in practice, we recommend adding additional examples. These examples could outline common scenarios entities may be faced with when considering what is an appropriate or inappropriate use of the exemption.

    (b) Add guidance to clarify how an entity that can apply the exemption should disclose actual performance of the acquisition or an example of the type of the required disclosures when an entity is applying the exemption.

Question 5

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?

Response to Question 5

Proposed disclosures about synergies (paragraphs B64(ea) and BC148-BC163)

19. The NZASB disagree with the proposed disclosures about expected synergies. This information is forward-looking and not aligned with the type of information generally included within general-purpose financial reporting for the reasons explained in our response to Question 1.

20. If these disclosures are required, we have concerns with the accuracy, completeness, verifiability and the cost to audit this forward-looking and highly judgemental information.

21. In our discussions with preparers on the ED proposals, they were concerned that it could be difficult to quantify synergies for the purposes of the proposed disclosures. They noted that during an acquisition, these synergies are not always predetermined and included in the rationale of the purchase price.

22. For instance, synergies from a business acquisition are not always identifiable, traceable and measurable. Synergy related to an acquisition may not fall within the acquired entities but in and across the consolidated group. Synergies may not be unlocked without other strategic changes. When performance of an entity improves, it is likely to be the result of several simultaneous causes and it is difficult (if not impossible) to isolate parts of the total effect to a specific cause (e.g. an acquisition).

23. The proposed disclosures will also require the collection and measurement of new information that will only be used for a very short period given the inherent limitations and subjective nature in forecasting synergies. Users will approach such information with caution, and we expect benefits to be minimal. Therefore, this information has a high marginal cost, while the reliability and subjectivity of the measures will also increase audit risk, time and effort.

24. Our constituents also raised their concern about the additional cost this type of disclosure would add to the audit. As this information is highly judgemental and forward looking there is a risk that management and the auditors will not agree.

25. From an audit perspective this has raised a question about the role of the auditor regarding this information, i.e. the level of work required to satisfy themselves to opine on the synergies from the acquisition.

26. We strongly recommend that the IASB does not proceed with the proposed disclosures on synergies. However, we have several further comments for IASB to consider if it must proceed:

(a) safeguards should be included in the guidance for the calculation of expected synergies. For example, referring to reasonable and supportable assumptions.

(b) it should be made clear that synergies may not necessarily equal or be readily reconcilable to the transaction price itself, and

(c) the requirements should specify what disclosures are required if no synergies are calculated at the time of acquisition.

Proposed amendments to paragraph B64(q) relating to the contribution of the acquired business (paragraphs BC166-BC177)

27. With the proposal to add the following text to paragraph B64(q)(ii): *'The acquirer shall develop an accounting policy to prepare this information that results in the acquirer disclosing information that helps users of its financial statements forecast future performance of the combined entity'* it is not clear how preparers should enhance their current approach to disclosing 'pro-forma' information considering the additional proposed requirement.

28. We suggest either adjusting the wording to make it clear what is required to be disclosed or adding an example of the disclosure or policy that is sufficient to satisfy this guidance.

Question 7

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?

Response to Question 7(a) Removing constraints on cash flows in value in use calculation (paragraphs BC204-BC214)

29. We recommend that the IASB considers whether retaining two different methods (value in use and fair value less costs of disposal) for calculating recoverable amount remains appropriate if the restrictions around cash flows for uncommitted restructurings and asset enhancements are removed from the value in use approach.

30. If the IASB maintains both methods, we recommend that examples are provided that illustrate the difference between the two methods.

Response to Question 7 (b) Allowing use of post-tax inputs (paragraphs BC215-BC222)

31. We agree with the proposal to remove the requirement to use pre-tax cash flows and pre-tax discount rates in the value in use calculation. Using post-tax inputs is more aligned with how value in use tends to be calculated in practice today.

Question 8

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?

Response to Question 8

32. We question the need for entities without public accountability to provide the proposed disclosures in paragraphs 36(da) and 36A of the Subsidiaries without Public Accountability Standard relating to expected synergies from business combinations. The necessity to quantify expected synergies might impose a significant reporting burden on these entities, which could outweigh the benefits of such disclosures to the users of their financial statements. Furthermore, as detailed in our response to Question 5, synergies cannot always be easily traced and could be distributed across the group rather than tied to the particular subsidiary.

33. Finally, paragraph BC255 explains that the IASB decided to require quantitative information about expected synergies on the basis the information is typically about an entity's short-term cash flows. We are concerned that expected synergies may not always relate to short-term cash flows (depending on their timing) and due to the subjective nature of these calculations does not provide an effective disclosure regardless. We consider that the costs of disclosing expected synergies far outweigh the benefits for entities without public accountability.