Staff paper

Agenda reference: 18B

IASB® meeting

Date	**December 2024**
Project	**Business Combinations—Disclosures, Goodwill and Impairment**
Topic	**Whether to require performance and expected synergy information**
Contacts	Akshaya Megharikh (akshaya.megharikh@ifrs.org) Dehao Fang (fdehao@ifrs.org)

Purpose and structure

1. As Agenda Paper 18 for this meeting explains, this paper:

   (a) summarises feedback on whether to require an entity to disclose information about the performance of a business combination and quantitative information about expected synergies; and

   (b) focusses on feedback that was common to the proposals to require an entity to disclose information about the performance of a business combination and quantitative information about expected synergies.

2. Feedback specific to each of these two proposed requirements is summarised in:

   (a) Agenda Paper 18C—Performance information—subset;

   (b) Agenda Paper 18D—Performance information—management approach and other feedback; and

   (c) Agenda Paper 18E—Expected synergies.

3. The paper is structured as follows:

   (a) key messages (paragraphs 4–6);

   (b) background (paragraph 7);

   (c) feedback summary (paragraphs 8–48); and

   (d) question for the IASB.

Key messages

4. There were divergent views, particularly between users and preparers on whether to require information about the performance of a business combination and quantitative information about expected synergies in financial statements.

   (a) almost all users agree with the proposal to require an entity to disclose information about the performance of a business combination and many users agree with the proposal to require an entity to disclose quantitative information about expected synergies. Users generally confirm the need for this information and say the information would help users assess management's decision to acquire businesses.

   (b) many preparers also acknowledge users' need for better information about business combinations and steps taken by the IASB since publishing the Discussion Paper to better balance users' need for this information with preparers' concerns. However, most preparers continue to disagree with requiring this information in financial statements.

5. Both organisations representing a group of securities regulators and some regulators support requiring the proposed disclosures while some regulators disagree. Feedback from auditors highlights concerns about a possible expectations gap that could arise as a consequence of requiring these disclosures in financial statements.

6. Respondents who disagree with requiring the proposed information in financial statements generally give the following main reasons:

(a) conceptual reasons;

(b) auditability and expectations gap;

(c) commercial sensitivity and litigation risks arising from disclosure of forward-looking information; and

(d) monetary costs and other concerns.

Background

7. The Exposure Draft *Business Combinations—Disclosures, Goodwill and Impairment* (Exposure Draft) proposed to require an entity to disclose information about:

(a) the performance of a strategic business combinations (performance information) including:

(i) an entity's acquisition-date key objectives and related targets (KOTs); and

(ii) the extent to which those KOTs are being met in subsequent periods; and

(b) quantitative information about synergies expected from combining the operations of an acquiree and an acquirer (expected synergy information) including a description of expected synergies by category and for each category of synergies:

(i) the estimated amounts or range of amounts of the expected synergies;

(ii) the estimated costs or range of costs to achieve these synergies; and

(iii) the time from which the benefits from the synergies are expected to start and how long they are expected to last.

Feedback summary

8. This section is structured as follows:

(a) trends in feedback (paragraphs 9–13);

(b) usefulness of information (paragraphs 14–16);

(c) stakeholder concerns:

  (i) conceptual concerns (paragraphs 20–21);

  (ii) auditability and expectations gap (paragraphs 22–31);

  (iii) commercial sensitivity and litigation risks arising from disclosing forward-looking information (paragraphs 32–40); and

  (iv) monetary costs and other concerns (paragraphs 41–43); and

(d) suggestions (paragraphs 44–48).

Trends in feedback

9. There were divergent views on whether to require disclosure of performance and expected synergy information.

10. Respondents who agree with requiring this information did not always specify why.

11. Some respondents who disagree with requiring this information in financial statements acknowledge users' need for better information about business combinations and steps taken by the IASB since publishing the Discussion Paper to better balance users' need for this information with preparers' concerns. However, these respondents say the measures do not go far enough to address their concerns.

12. We identified the following trends by respondent types:

(a) almost all users and user groups agree with requiring an entity to disclose performance information and most users and user groups agree with the requiring an entity to disclose expected synergy information;

(b) most preparers and preparer groups disagree with requiring an entity to disclose performance information and almost all preparers and preparer groups disagree with requiring an entity to disclose expected synergy information;

(c) both organisations representing a group of securities regulators and some regulators agree while some other regulators disagree with requiring an entity to disclose performance and expected synergy information.

13. We identified the following trends by geography:

(a) there was greater disagreement among respondents from Europe and Americas than respondents from Asia-Oceania and Africa; and

(b) many respondents representing global or regional organisations agree.

Information usefulness

14. Many respondents who agree with requiring disclosure of performance and expected synergy information in financial statements say the information would be meaningful and would help users assess the performance of business combinations.

15. Many users and user groups say business combinations tend to be risky, often failing to achieve their goals, and the proposed information would help them better assess management's performance. Many users say entities sometimes provide information similar to information that would be required by the Exposure Draft when announcing an acquisition, but do not follow-up on that information and the information is often no longer available after the business combination is completed.

16. Some respondents disagree and say performance and expected synergy information is unlikely to be useful because:

(a) management would be reluctant to disclose commercially sensitive information (see paragraphs 32–35), potentially leading to boiler plate disclosures.

(b) other information could be more useful—paragraphs 13–19 of Agenda Paper 18A explains suggestions for alternative requirements, for example amortising goodwill or enhancing disclosure requirements of IAS 36 *Impairment of Assets*.

(c) market conditions and management's views that exist at the acquisition date might not be reflective of conditions and views at the time of reporting.

(d) internal information used for management purposes, such as aspirational targets to motivate employees (see paragraph 21(e)), might not be relevant for users in making investment decisions.

(e) the information could be misleading in some situations—for example, a few respondents say failing to achieve a key objective for a business combination might mislead users into viewing a business combination as unsuccessful when that might not be the case. This could happen, for example, when there may be multiple acceptable outcomes for an entity when entering into a business combination. These respondents read the requirements as forcing an entity to designate the achievement of one of those possible outcomes as the key objective and say doing so would not provide users with the full picture of acceptable alternative outcomes.

Concerns[1]

17. Many respondents raise concerns about requiring disclosure of performance and expected synergy information in financial statements. Many preparer and preparer groups say the costs to provide this information would outweigh the benefits. Some respondents, mostly preparers, say existing disclosure requirements in IAS 36 and IFRS 8 *Operating Segments* suffice in providing users information they need. In their view, the IASB should not increase preparers' burden by proposing new disclosures.

18. Respondents raise the following concerns:

(a) conceptual concerns (paragraphs 20–21);

(b) auditability and expectations gap (paragraphs 22–31);

[1] This section discusses concerns other than those related to the usefulness of performance and expected synergy information which paragraph 16 discusses.

(c) commercial sensitivity and litigation risk arising from disclosing forward-looking information (paragraphs 32–40); and

(d) monetary costs and other concerns (paragraphs 41–43).

19. Respondents' suggestions for how to address these concerns are summarised in paragraphs 44–48.

Conceptual concerns

20. Paragraphs BC138–BC141 of the Basis for Conclusions on the Exposure Draft (Basis for Conclusions) explain that:

(a) in the IASB's view, most of the information that would be required by the proposals is not forward-looking because it reflects assumptions made about the business combination at the acquisition date and not expectations of the future as at the reporting date or when the financial statements are issued.

(b) even if the information is forward-looking, paragraph 3.6 of the *Conceptual Framework for Financial Reporting* (Conceptual Framework) does not prohibit the requirement of such disclosure because it:

(i) relates to the assets acquired and liabilities assumed in the business combination; and

(ii) is useful for users.

21. Some respondents disagree and say performance and expected synergy information should not—from a conceptual perspective—be required in financial statements. They say:

(a) performance and expected synergy information is forward-looking. Paragraph 3.6 of the Conceptual Framework says forward-looking information is typically not included in financial statements and they do not see a reason to make an exception in this case.

(b) performance information does not directly relate to the entity's assets, liabilities, equity, income and expenses. In particular:

   (i) disclosures applying other IFRS Accounting Standards are clearly linked to amounts recognised in the financial statements—for example, assumptions about the expected credit losses of a financial asset;

   (ii) goodwill is measured as a residual so there is no direct link between goodwill recognised and management's assumptions about expected synergies or KOTs for a business combination; and

   (iii) the measurement of goodwill can be affected by factors not directly linked to the value management expects from a business combination—for example, if the fair value of consideration paid in shares changes between the announcement and acquisition dates.

(c) paragraph 1.6 of the Conceptual Framework says general purpose financial statements 'do not and cannot provide all information that [users] need…'. In these respondents' view, information being relevant to users is not a sufficient reason to require an entity to disclose information in financial statements.

(d) the rationale for requiring disclosure of performance and expected synergy information in financial statements (see paragraph 20) would also apply to similar information for many other types of transactions—such as capital expenditure in pursuit of organic growth—and the proposals could potentially open a 'flood gate' for any information remotely related to an asset or liability to be included in the financial statements.

(e) the nature of management's internal targets for a business combination could differ from the nature of other information typically disclosed in financial statements. Management may often set aspirational internal targets for a business combination to encourage certain behaviours, rather than to serve as an unbiased estimate of future outcomes or of what is reasonably achievable (for example, sales targets used to determine employee remuneration). This information, if disclosed in financial statements, might not faithfully represent what it purports to represent.

Auditability and expectations gap

22. Paragraphs BC144–BC145 in the Basis for Conclusions say the IASB expects auditors and regulators will be able to verify:

    (a) whether the information disclosed is the information an entity's key management personnel receive to review a business combination;

    (b) whether there is adequate explanation and appropriate evidence supporting the information; and

    (c) whether the information disclosed faithfully represents what it purports to represent.

23. Many respondents raise concerns around auditing the performance and expected synergy information, including:

    (a) audit expectations gap (paragraphs 25–28); and

    (b) auditability concerns (paragraphs 29–31).

24. Some respondents suggest collaborating with the International Auditing and Assurance Standards Board (IAASB) to develop a solution for the auditing the information.

Audit expectations gap

25. Accounting firms agree they would be able to verify whether the information disclosed by an entity is information management received to review a business combination. Respondents confirm it would be difficult to verify the reasonableness of the information (including the appropriateness and achievability of KOTs and expected synergies).

26. However, some respondents, including many audit firms, accounting bodies and standard setters highlight a possible expectations gap that could arise as a consequence of requiring this information in financial statements. Some of these respondents acknowledge the IASB is not expecting auditors to verify the reasonableness of the information. However, they say users might misunderstand the audit work done and conclude that auditors have audited the reasonableness of the information. They say users might place undue weight on the reasonableness of such information when that information is included in the audited financial statements.

27. One Interpretations Committee member says the expectation gap would be pronounced when it comes to information about an entity's actual performance in subsequent periods. In this respondent's view, users could understand that the acquisition-date disclosures reflect management's expectation at the time of the transaction. However, because information about actual performance in subsequent periods is historical information, a user would expect an auditor to audit the reasonableness of this information. However, doing so could be challenging, particularly if the key objectives or targets are qualitative or are based on measures not defined in IFRS Accounting Standards.

28. Some respondents provide suggestions to manage the expectations gap. Paragraph 45 discusses those suggestions.

Auditability concerns

29. Many respondents raise concerns about the cost to audit the performance and expected synergy information. Respondents say the information required by these disclosures can be highly subjective, requiring audit firms to perform extensive audit procedures, leading to significant increases to audit costs. Respondents also say entities might need to incur significant costs to establish new systems or controls that can be audited (see paragraph 41).

30. A few respondents say paragraph BC145 of the Basis for Conclusions (see paragraph 22) is unclear on whether the IASB expects an audit to cover the reasonableness of the

information. A few say management's targets for a business combination might often be aspirational and therefore not represent management's reasonable expectations. These respondents suggest not including the IASB's observation in paragraph BC145(c) of the Basis for Conclusions about auditors being able to verify whether the information disclosed faithfully represents what it purports to represent in any final amendments.

31. On the other hand, some preparers say an audit that merely confirms management's review of the information—without assessing its reasonableness or appropriateness—might not be beneficial to users.

Commercial sensitivity and litigation risks arising from disclosing forward-looking information (proprietary costs)

Commercial sensitivity and proposed exemption

32. In the Exposure Draft, the IASB proposed to exempt an entity from disclosing some information about the performance of a business combination and expected synergies if specific conditions are met. The proposed exemption was designed to respond to some concerns about commercial sensitivity.

33. Many respondents, including many preparers, preparer groups and some accounting standard setters say performance and expected synergy information could be commercially sensitive and that disclosing this information could cause the entity harm. Users and user groups also agree that there could be circumstances in which disclosing information could harm an entity and that it would be appropriate to exempt an entity from disclosing that information. This may be the case, for example, if an entity undertakes a business combination to launch a new product.

34. Among these respondents:

    (a) many acknowledge the proposed exemption but say the exemption would not adequately address concerns about commercial sensitivity; and

(b) many say the information could be commercially sensitive but do not elaborate further or comment on the interaction with the proposed exemption.

35. Agenda Paper 18F summarises feedback on the proposed exemption.

Litigation risks from disclosing forward-looking information

36. Paragraph BC142 of the Basis for Conclusions on the Exposure Draft states:

> …the IASB acknowledges that other stakeholders regard the information to be forward-looking, possibly because of different definitions of forward-looking in local regulations. The definition of forward-looking information in those regulations might result in additional litigation risk for an entity disclosing the information. The IASB considered this feedback in developing the exemption …

37. Some regulators say information about KOTs and expected synergies would be regarded as forward-looking in their jurisdictions and requiring such information in the financial statements could:

(a) result in an entity losing the protection from safe-harbour provisions[2] and expose them to undue litigation risks. These regulators say local regulations would need to be amended if the IASB finalises the proposals.

(b) be incompatible with local regulations—one regulator says local regulations may prohibit an entity from providing forward-looking information unless the information is provided in a specific format and/or includes specific statements. The regulator says disclosing the information that would be required applying the IASB's proposal without providing the specific format or statements required by local regulations would not conform to those regulations.

[2] Some jurisdictions offer entities 'safe-harbour' protections, which will protect entities from litigation for information disclosed in documents such as a management commentary but not from information disclosed in financial statements.

38. Some preparers and preparer groups also raise concerns about potential litigation risks that may arise from disclosing the information in financial statements. They say an entity may fail to achieve its KOTs for reasons outside of the entity's control and that the proposed disclosures could lead to litigation which may be costly for entities even if the entity successfully defends itself.

39. A few respondents acknowledge the proposed exemption but say it does not fully address concerns about litigation risks (Agenda Paper 18F summarises feedback on the proposed exemption).

40. Some respondents made suggestions to help mitigate litigation risk (in addition to their suggestions on the proposed exemption which Agenda Paper 18F for this meeting discusses). Paragraph 45 discusses these suggestions.

Monetary costs and other concerns

41. In addition to costs required to audit performance and expected synergy information (see paragraph 29), some respondents say entities might not have appropriate systems and controls in place to produce performance and expected synergy information that would stand up to the scrutiny of an audit. They say although the information might be internally available, entities would be required to establish new systems and controls to formalise the process which could involve significant costs.

42. However, one preparer says the proposal could help the finance department take back control over the preparation of performance and expected synergy information which could enhance the reliability of the information.

43. Respondents also raise some other concerns about requiring performance and expected synergy information in financial statements:

    (a) a few preparers and preparer groups, mostly from Europe, say the proposals, if finalised, could affect the competitiveness of entities applying IFRS Accounting Standards if entities applying US GAAP would not be required to disclose similar information.

(b) a few preparers say the information might not be readily available. For example, one preparer says an entity might not always have KOTs for a business combination even if that business combination is strategic. This could happen, for example, when a government forces an entity to take over a competitor within a short time frame.

(c) a few respondents say an entity might not have sufficient time to gather and disclose the information, especially if the business combination occurs close to financial year-end.

(d) a few respondents suggest considering exempting an entity from disclosing performance and expected synergy information in interim financial reports. One respondent says information reported internally about business combinations might not be in line with quarterly reporting cycles.

(e) one preparer group says regulations in its jurisdiction require an entity to provide specific information at the time of a business combination. The information provided could be different from what the proposals in the Exposure Draft would require. In its view, differences in the information provided in different documents could confuse users.

(f) one preparer group expresses concern about the potential unintended consequences of the proposals, due to focusing solely on business combinations. They say the proposed requirements, if finalised, might deter companies from pursuing growth through business combinations and focus solely on organic growth.

Suggestions

44. Many respondents say performance and expected synergy information would be better suited outside an entity's financial statements, for example in management commentary. Many of these respondents suggest the IASB consider whether such information should be provided as part of its Management Commentary project because performance and expected synergy information is, in their view, similar to

information typically provided in an entity's management commentary. These respondents say providing the information outside of an entity's financial statements:

(a) would allow preparers flexibility to tailor information in a way that would provide users with the bigger picture while minimising the impact of disclosing information that could be commercial sensitive or forward-looking.

(b) would address concerns about audit expectations gap, auditability of information and costs because:

   (i) in most jurisdictions, information disclosed outside of the financial statements is not subject to audit; and

   (ii) entities could avoid the need to establish new systems and control processes required to produce information capable of withstanding audit scrutiny.

45. To manage the audit expectations gap (see paragraphs 25–28) and mitigate litigation risk that might arise from disclosing performance and expected synergy information (see paragraphs 36–40):

(a) some respondents suggest requiring an entity to:

   (i) explicitly state in the financial statements that the disclosed KOTs and expected synergies are:

      1. solely based on information used and prepared by management based on their acquisition-date best estimates; and

      2. those expectations might not be realised in the future and might not be comparable to similar measures provided by other entities;

   (ii) a few respondents suggest requiring an entity to disclose the basis of preparation for any targets based on measures not defined in IFRS Accounting Standards; and

   (iii) a few respondents suggest providing further guidance and illustrative examples to assist preparers and auditors.

46. A few respondents suggest field testing the proposed requirements to disclose performance and expected synergy information.

47. Some respondents suggest requiring performance and expected synergy information only for entities with public accountability or those that are listed. These respondents say the cost of disclosing performance and expected synergy information would outweigh the benefits for smaller, private entities. A few respondents from Latin America suggest consolidating all disclosure requirements that are relevant for only listed entities as part of a separate project.

48. A few respondents suggest requiring entities to disclose only qualitative information about performance and expected synergies. In their view, such an approach would offer entities flexibility to avoid practical challenges that they might encounter for disclosing quantitative information. The approach would also allow entities to disclose the information in a manner that would be more understandable and could provide users better information about the bigger picture.

Question for the IASB
Do IASB members have any questions or comments on the feedback in this agenda paper?