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Business Combinations: Disclosures, Goodwill and Impairment

Other aspects of the management approach Issues Paper

Objective

- 1 To ask EFRAG FR TEG members for their views on the IASB's tentative decisions on the following aspects of the management approach when disclosing information about the objectives and subsequent performance of a business combination:
 - (a) How long information should be required for
 - (b) Changing metrics
 - (c) Use of ranges; and key objectives
- 2 This paper is based on the [IASB Agenda Paper 18B](#) discussed at the IASB meeting in February 2023.
- 3 Questions to EFRAG FR TEG are at the end of this paper (paragraph 50).

Background

- 4 The IASB issued the Discussion paper [Business Combinations – Disclosures, Goodwill and Impairment](#) ('the DP') in March 2020 with a comment period that ended on 31 December 2020.
- 5 In February 2023, the IASB tentatively decided that an entity disclose information about the objectives and subsequent performance of business combinations applying a 'management approach'. This means that the information an entity would be required to disclose is the information the entity's management uses in assessing and monitoring the business combinations post-acquisition. This is discussed in agenda paper 04-02 for this session.

Structure of this paper

- 6 This paper is structured as follows:
 - (a) How long is the information required for
 - (b) Changes metrics
 - (c) Use of ranges and key objectives

How long information should be required for

Proposals in the DP

- 7 Paragraph 2.44 of the DP explains that:

- (a) if an entity's chief operating decision maker (CODM) continues to monitor whether the objectives of a business combination are being met, the entity should disclose information about the subsequent performance of that business combination for **as long as the information remains necessary** for users of financial statements (users) to assess whether the original objectives of a business combination are being met (**the core time period**); and
- (b) if management of an entity:
 - (i) does not monitor whether its objectives for a business combination are being met, the entity should disclose that fact and the reasons why it does not do so; and
 - (ii) stop monitoring a business combination before the end of the second full year after the year in which the business combination occurs, the entity should disclose that fact and the reasons why it stopped monitoring the business combination (**the overlay**).

Feedback on the proposals

Feedback to the IASB

- 8 There were mixed views on the core time period proposed in the DP. Some respondents agreed with the core time period. However, a few respondents suggested that an entity should be required to disclose the required information for a specified time period:
- (a) a fixed time period, such as two or five years.
 - (b) the period for which synergies arising from the business combination are expected to be realised or the period until integration of the business combination is completed.
- 9 Other comments and suggestions made by some respondents to the DP included:
- (a) The core time period would be short for some business combinations because the CODM is likely to monitor subsequent performance of a business combination against initial management's objectives and targets for only a short period to ensure that integration is happening successfully. However, the success or failure of some business combinations might not be apparent for many years (for up to 20 years after the business combination took place). Those respondents said requiring entities to disclose information only in the first few years after a business combination might encourage short-term behaviours that do not add value in the longer term.
 - (b) The CODM reviews information about the performance of a business combination for between two and five years.
 - (c) The CODM reviews the performance of a business combination against the business plan developed during the acquisition process for only up to one year after the business combination. After that, the business combination is monitored as part of the entity's annual budgeting process and therefore the CODM reviews the performance of the business as a whole (including the acquired business) against an updated business plan instead of the assumptions made at the time of the business combination.
- 10 On the overlay, most respondents who commented agreed with the IASB's preliminary view to require an entity to disclose if the entity's management (CODM) has stopped monitoring a business combination.

EFRAG Final Comment Letter

- 11 In its Final Comment Letter, EFRAG generally agreed that it would be useful for an entity to disclose:

- (a) whether it is meeting the objectives as long as it continues to monitor the acquisition – or the fact that it is not monitoring an acquisition;
 - (b) if it stops monitoring, whether the objectives are being met; and
 - (c) if it changes the metrics it uses, to monitor whether the objectives of the acquisition are being met.
- 12 EFRAG noted that the requirement to disclose when an acquisition is not monitored could perhaps discourage some entities from such an approach. In other words, the requirement to disclose that an entity is not monitoring an acquisition could create a market discipline.
- 13 EFRAG assessed that after two to three years, it may be difficult, for practical reasons, to monitor whether the objectives of an acquisition have been met, because of integration. However, as the integration could take more than two years for a significant proportion of material acquisitions. EFRAG considered that an entity should disclose if it stops monitoring. In EFRAG's view, an entity should also disclose whether the objectives of an acquisition have been met within the first three years following the acquisition, instead of after the two years suggested in the DP.
- 14 EFRAG added that if an entity assesses that it is useful to continue to monitor the acquisition for a longer time, this information is also likely to be useful for the users of financial statements. If the information is to be provided, EFRAG, therefore, also supported that the entity should continue to disclose whether the objectives for an acquisition are being met as long as this is monitored by the management of the entity.
- 15 EFRAG agreed with the proposals that an entity should not be required to provide metrics about an acquisition if such metrics are not monitored by the management. This is because it will not always be meaningful to provide such metrics.

IASB Staff analysis

- 16 Based on the feedback received, the IASB Staff concluded that the IASB should confirm its preliminary view in the DP and require an entity to disclose information for however long the entity's management monitor whether the objectives of the business combination are being met. This is because:
- (a) doing so would require an entity to disclose information based on what is available internally to an entity's management. This information should be less costly because the information already exists.
 - (b) doing so caters for the fact that the management of different entities review the subsequent performance of business combinations differently.
 - (c) doing so would capture ad-hoc information reviewed by an entity's management—for example from 'post-acquisition reviews'.
 - (d) any fixed time period would be arbitrary and be subject to feedback similar to that received on the overlay.
- 17 Regarding the overlay, the IASB Staff considered that the IASB should proceed with the overlay. In the view of the Staff such information would be useful for users. Part of the IASB's reason for requiring entities to disclose information about the subsequent performance of a business combination is to help users assess management's stewardship of an entity's economic resources. Users have said that knowing that an entity's management is not monitoring or has stopped monitoring the performance of what can be significant and risky investments is relevant in their assessment of management's stewardship.
- 18 The IASB Staff acknowledged that the time period for this overlay is somewhat arbitrary and considered that it is not possible to set a time period that would satisfy

all stakeholders. Given the feedback, the IASB Staff consider the year of the business combination and the two subsequent full years remains appropriate.

- 19 Therefore, the IASB staff recommended the IASB to:
- (a) proceed with its preliminary view in the DP regarding the core time period and the overlay.
 - (b) propose an entity whose management stops monitoring the performance of a business combination before the end of the second full year after the year of the business combination be required to disclose information about actual performance using the metric set out in the year of acquisition if (and only if) information about actual performance using that metric is being received by the entity's management.

IASB tentative decisions

- 20 The IASB generally supported the IASB Staff analysis and recommendations and tentatively decided:
- (a) to **maintain its preliminary view** that an entity be required to disclose information about the subsequent performance of a business combination for as long as the entity's management continues to monitor whether the objectives of the business combination are being met (that is, the entity's management compares actual performance with the entity's objectives and targets for the business combination it established when entering into the business combination).
 - (b) to **maintain its preliminary view** that if an entity's management does not monitor whether its objectives for a business combination are being met, the entity should disclose that fact and the reasons why it does not do so.
 - (c) to **maintain its preliminary view** that if an entity's management stops monitoring, before the end of the second full year after the year of the business combination, whether its objectives for a business combination are being met, the entity should disclose that fact and the reasons why it has done so.
 - (d) to propose that an entity whose management stops monitoring, before the end of the second full year after the year of the business combination, whether its objectives for a business combination are being met, **be required to disclose information about actual performance**. The entity will be required to disclose information using the metric set out in the year of acquisition, if (and only if) information about actual performance using that metric is being received by the entity's management.

- 21 All 12 IASB members agreed with these decisions.

EFRAG Secretariat observations

- 22 The EFRAG Secretariat considers that the IASB tentative decisions are broadly in line with EFRAG's views in its Final Comment Letter. The one point that is different is that EFRAG considered that it should be disclosed if an entity stops monitoring whether the objectives of an acquisition have been met within the first three years following the acquisition, instead of after the two years suggested in the DP (see paragraph 13).

Changing metrics

Proposals in the DP

- 23 Paragraph 2.21 of the DP discusses situations in which the metrics management use to monitor the subsequent performance of a business combination change over time—for example, when an entity is reorganised.

- 24 Paragraph 2.21 explains that the IASB considered it unreasonable to require an entity to continue disclosing metrics that no longer provide useful information to management or that are no longer available internally. However, changing the metrics without disclosing the reasons for that change could allow poor performance to be masked. To balance these concerns, the IASB's preliminary view was that **it should not require an entity to continue disclosing a metric it no longer uses internally**. Instead, when an entity makes such a change, it should be required to disclose:
- (a) that it made the change;
 - (b) the reasons for the change; and
 - (c) the revised metrics.

Feedback on the proposals

IASB feedback

- 25 The IASB received mixed feedback on changing metrics. Most respondents who commented agreed with this preliminary view in the DP.
- 26 However, some respondents - primarily accounting bodies and national standard-setters but also a few users - expressed concern that permitting entities to change the metrics would:
- (a) reduce comparability of the financial statements over time; and
 - (b) allow entities to mask poor performance by disclosing a better performing metric instead.
- 27 Feedback from the IASB Staff fieldwork conducted post-DP supported the IASB preliminary view. Entities typically obtain much more detailed information after the business combination, and this can lead to the acquirer's management reassessing the expected benefits and changing its targets.

EFRAG Final Comment Letter

- 28 EFRAG agreed that it would be useful for an entity to disclose if it changes the metrics it uses to monitor whether the objectives of the acquisition are being met.
- 29 EFRAG considered that it would seem inconsistent from a cost/benefit perspective to require companies that change the metrics used, to keep monitoring the acquisition based on the old metrics, while companies that stop monitoring whether the objectives for the acquisition are being met are not required to do so.
- 30 Requiring companies to disclose the new metrics and the reasons for the change, would thus seem to be a good balance. While the new metrics may not provide useful information to assess whether the objectives of an acquisition have been met, the companies' disclosure of the reason for the change and the new metrics could be useful.

IASB Staff analysis

- 31 The IASB Staff noted that most respondents agreed with the IASB's preliminary view to allow an entity to change the metrics its management uses to monitor whether a business combination met its objectives. Some of those respondents highlighted that information about management changing metrics and about the new metrics is useful to communicate changes in the entity's objectives for the business combination.
- 32 The IASB Staff considered that the IASB preliminary view described in paragraph 2.21 of the DP was meant to provide relief to entities from having to disclose information in subsequent periods only when disclosing information based on the

original metrics would be impracticable. In some cases, like a reorganisation could result in information about a particular metric no longer being available.

- 33 Applying the preliminary view, if an entity's management changes its targets for a business combination for reasons other than impracticability, management would no longer be considered to be monitoring the subsequent performance of the business combination. The entity would therefore no longer be required to disclose information about the subsequent performance of the business combination. Additionally, if this happens during the two-year overlay period, the entity would be required to disclose the information.
- 34 Overall, the IASB Staff did not think it would be useful for an entity to disclose if it changes the metric used and the reasons for the change and recommended the IASB not to proceed with its preliminary view.

IASB tentative decisions

- 35 The IASB supported the IASB Staff recommendation in paragraph 33 and tentatively decided **not to proceed with its preliminary view** to require an entity to disclose if it changes the metric used and the reasons for the change.
- 36 Seven of 12 IASB members agreed with this decision.
- 37 The IASB members that disagreed noted that users would be losing information if an entity did not inform that it had changed the metric it originally set to monitor the business combination. These IASB members also said that most respondents to the DP had agreed with the preliminary view, and hence did not see a good reason to change it.

EFRAG Secretariat observations

- 38 The EFRAG Secretariat does not see a valid reason why the IASB did not confirm its preliminary view given that most respondents, including EFRAG, supported the proposal to require an entity to disclose if it changes the metric used and the reasons for the change on the basis that this would provide useful information to users of financial statements.

Use of ranges and key objectives

Proposals in the DP

- 39 In addition to the IASB's preliminary view about the subsequent performance of business combinations, the IASB also considered requiring an entity to disclose quantitative information about synergies expected from a business combination (expected synergies).
- 40 Paragraph 2.91 of the DP notes that quantitative information about expected synergies could be the 'estimated amount or range of amounts of the synergies'. However, the DP is silent as to whether information about an entity's targets for a business combination can be disclosed as a range rather than a point estimate.
- 41 Paragraph 2.12 of the DP describes the objectives an entity would need to disclose as 'the objectives of the acquisition that management considers must be achieved for the acquisition to be a success'.

Feedback on the proposals

IASB feedback

- 42 Some preparers asked if an entity could disclose their targets for the business combination as a range. Those preparers said assumptions for pricing a business combination, as well as management's targets for a business combination, are often estimated as a range rather than precise amounts. Several preparers asked about the level of detail about the objectives.

EFRAG Final Comment Letter

- 43 EFRAG suggested the IASB to further clarify how they consider the disclosures to be provided, and what 'synergies' encompass. EFRAG also considered that the IASB should further examine whether the disclosures would be better provided in the management commentary, taking into account both the concerns about including some of the proposed information in the financial statements and the concerns related to allowing the information to be provided in the management commentary. Similar to disclosures on management objectives for an acquisition and its subsequent performance, EFRAG notes that the IASB would have to consider how to avoid entities having to disclose commercially sensitive information.

IASB Staff analysis

- 44 Given the feedback received, the IASB Staff considered that the IASB should clarify that information about an entity's target for a business combination could be disclosed as a range or as a precise amount.
- 45 Similar to expected synergies, the IASB Staff acknowledged some targets can be difficult to estimate with precision and therefore management might only estimate those targets as a range.
- 46 Regarding the key objectives the IASB Staff:
- (a) noted that a common concern about disclosing information about the subsequent performance of business combinations is that the information could be commercially sensitive. The IASB Staff think that an additional factor contributing to this concern may have been a perception about being required to disclose detailed information about an entity's objectives for a business combination.
 - (b) the IASB staff therefore recommended the IASB to clarify that information about an entity's objectives and targets for a business combination should focus only on the key objectives - that is, the objectives that are critical to the success of the business combination. An entity would not be expected to disclose all objectives and targets for a business combination.

IASB tentative decisions

- 47 The IASB tentatively decided:
- (a) to permit an entity to disclose information about its targets for a business combination as a range or a point estimate.
 - (b) to clarify that an entity will be required to disclose only information about its key objectives—that is, the objectives critical to the success of the business combination.
- 48 All 12 IASB members agreed with these decisions.

EFRAG Secretariat observations

- 49 The EFRAG Secretariat notes that although EFRAG did not specifically question the range as described in the DP, we think that disclosing the information required in a more aggregated way (where less details are provided) as suggested in the IASB tentative decision might help address the concerns around commercial sensitivity of information. We also consider that the IASB tentative decision to clarify that the focus is on key objectives is helpful from a cost-benefit perspective.

Questions for EFRAG FR TEG

- 50 What are your views on the IASB tentative decisions in the following paragraphs:
- (a) How long information should be required for – **paragraph 20**
 - (b) Changing metrics – **paragraph 35**
 - (c) Use of ranges and key objectives – **paragraph 47**