ASSOCIATION DES BANQUIERS CANADIENS
CANADIAN BANKERS ASSOCIATION

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July 15, 2024

Mr. Andreas Barckow, Chair
International Accounting Standards Board
Columbus Building
7 Westferry Circus
Canary Wharf
London, E14 4HD
United Kingdom

Dear Mr. Barckow,

RE: Invitation to Comment - Business Combinations - Disclosures, Goodwill and Impairment Exposure Draft (ED/2024/1)

The Canadian Bankers Association ("CBA")[1] would like to thank the International Accounting Standards Board ("IASB" or the "Board") for the opportunity to comment on the *Business Combinations—Disclosures, Goodwill and Impairment* Exposure Draft (the "ED"). We understand that the Board is publishing this ED to seek the views of stakeholders on its proposals for amended disclosure requirements on business combinations, goodwill and impairment, in order to provide users with more useful information about business combinations at a reasonable cost. In particular, we appreciate the Board's proposals to improve the goodwill impairment testing process by permitting the inclusion of cash flows from future restructurings and the use of after-tax discount rates, which will reduce the cost and complexity of preparing key assumptions for the value-in-use calculation.

In this letter, we highlight our support for certain of the IASB proposals as well as indicate our key areas of concern and recommendations to address them. As such, we have not provided individual responses to the consultation questions in the ED, as we believe our comments contained herein (which reference the questions) address them.

Executive Summary—Key Themes

We urge the Board to reconsider its proposal to require disclosure on the key objectives and targets of strategic business combinations and on the expected synergies in the year of acquisition, especially if the disclosures are commercially sensitive and not practical to apply. We are also concerned that while these disclosures may be relevant to users, the information disclosed will not be sufficiently reliable to be useful, due to the significant judgment, estimates and assumptions involved. Extending from this, we believe that the requirement to provide information about the expected benefits of strategic acquisitions is a form of future orientated financial information (FOFI) that should not be included in historical financial statements due to concerns about objectivity, quality of information, and auditability.

If the IASB moves forward with the disclosure requirements, we agree that the use of a threshold is useful to limit the application to the most material acquisitions, although we believe that the threshold should be increased to focus on truly strategic acquisitions. We also request more guidance and illustrative examples on the application of the qualitative criteria. As well, we believe that the exemption criteria should be broadened to better protect information that is confidential and/or sensitive either commercially or from a regulatory perspective (e.g., competition). We also suggest that the targets disclosed should be limited to targets that are financial measures calculated pursuant to IFRS or easily reconciled to IFRS. We have included recommendations below with respect to these points to increase the practical application of the requirements.

[1] The CBA is the voice of more than 60 domestic and foreign banks that help drive Canada's economic growth and prosperity. The CBA advocates for public policies that contribute to a sound, thriving banking system to ensure Canadians can succeed in their financial goals. www.cba.ca.

With respect to the proposed changes to the impairment test, we do not believe that the concerns on shielding in goodwill impairment testing should be addressed by amending the guidance for allocating goodwill to cash generating units (CGUs), as this proposed approach may not be feasible or necessarily provide more relevant information for legacy acquisitions and may require restructuring internal management reporting to align with the new definitions, adding further costs and complexity.

We also suggest that the Board reconsider addressing the concerns on the continuous monitoring of the measurement of goodwill through an accounting requirement to amortize goodwill over a specified period of time as a more practical alternative to complex and voluminous disclosure requirements.

IFRS 3 Disclosure Proposals

Disclosure of quantitative information about expected synergies (Question #5)

We recommend that the Board reconsider the proposed requirement to disclose the estimated amount or range of amounts of the synergies and the estimated cost or range of costs to achieve those synergies, because these disclosures may reveal confidential strategic information, may not be practical to estimate in the context of financial reporting, and represent forward looking estimates that may require significant judgment.

Disclosing subjective internal estimates of the synergies of an acquisition and the related costs will require the application of significant judgment and assumptions and may result in lower quality information than historical financial information, limiting its reliability and usefulness. The inclusion of this type of forward-looking information will also add significantly to the effort and complexity of auditing these disclosures, thereby increasing the cost of preparing the disclosures. As well, to the extent that auditors are not able to get comfort over this forward-looking information and the underlying assumptions, it may reduce the scope of the information ultimately disclosed. Depending on the acquisition, the synergies may also not reside solely within the acquiree and may also benefit other entities or operations within the consolidated group, which may result in the disclosure of confidential or commercially sensitive information for operations beyond those of the acquiree. In addition, the information could be considered forward-looking information under securities law in certain jurisdictions, which may expose entities to additional regulatory and litigation risk.

We would instead recommend enhancing the qualitative disclosures, by expanding on the existing requirements IFRS 3.B64(e), which require disclosure on the factors that make up the goodwill recognized, such as the expected synergies. To the extent that quantitative disclosure requirements are retained, we suggest the Board consider replacing the disclosure of synergies (whether revenue or cost synergies) with the disclosure of the estimated incremental revenues and operating profits. These measures may be less complex to prepare and would provide more useful and objective information to users to estimate the value of the combined business. We also recommend that any quantitative disclosures be limited to strategic business combinations, as defined in the ED, given both the limitations and complexities of providing this disclosure, as discussed above, and because the information may have limited value without the corresponding disclosures proposed in the ED for strategic business combinations on the actual performance in subsequent reporting periods.

Disclosures on the Performance of a business combination (Question #1)

We recommend that the Board reconsider the proposal to require disclosure of the acquisition-date key objectives and targets for strategic business combinations, both at the acquisition-date and in subsequent reporting periods.

While we agree with the objective of providing users with information about the performance of a business combination, we believe that the concerns about reliability, commercial sensitivity, and the costs of making such disclosures would outweigh the incremental benefits of applying these amendments. As discussed above, developing this type of forward-looking information will require significant judgment,

estimates and assumptions, and may produce information with limited usefulness and auditability. Information regarding business combinations, specifically acquisition-date key objectives and related targets, is also commercially sensitive in many cases. Including such information could provide other potential acquirees or competitors with insight into how an entity prices strategic acquisitions. Disclosure of targets supported by expected expense synergies would provide undue insight into an entity's internal cost structure, and disclosure of targets supported by expected revenue synergies would provide undue insight into an entity's client acquisition and retention strategies. It is unclear whether the exemption would in practice limit the disclosure of this information. Even if the confidential nature of this information results in the application of the exemption, this would involve additional cost for preparers to prove that the exemption is applicable, with limited resulting benefit to users.

The determination of the targets may also not be possible when the acquired business is subject to high levels of integration with the purchaser. Many acquisitions are fully or partially integrated with an existing business and monitored by management at the level of the combined business, up to and including at the operating segment level. To the extent that the existing business is significantly larger than the acquisition, or the nature and risks of the existing and acquired business differ, the results of the combined business may not provide a useful metric for assessing the subsequent performance of an acquisition. In addition, some of the requested details to be disclosed would require forward-looking estimates that are highly judgmental and therefore more complex for an auditor to verify, increasing the cost of providing these disclosures.

Although the proposed disclosure is subject to an exemption, the determination of whether the exemption can be applied requires significant judgment and may also pose a challenge for auditors to verify whether the exemption has been appropriately applied. The proposed exemption is also too narrow in scope to address the concerns noted above with respect to confidentiality and the sensitivity of the information due to commercial or regulatory considerations. Please see the "Exemption from Disclosing Information" section below for additional commentary on the exemption.

We suggest that the quantitative disclosures on expected and actual performance be replaced with additional qualitative disclosure requirements on the potential risks and opportunities associated with the acquisition, and the extent to which those are being achieved post-combination. This would provide users with insight into the effectiveness of the entity's acquisition and how it aligns with the acquirer's strategy, while balancing the costs and risks of disclosing forward-looking and commercially sensitive information.

If the quantitative disclosure requirements are retained, we recommend that the key objectives and targets be disclosed at a greater level of aggregation, such as for the combined entity post-acquisition, to better align with other reporting of the entity and protect information that is confidential and/or sensitive commercially or from a regulatory perspective (e.g., competition). We also recommend that the targets disclosed be limited to targets that are financial measures calculated pursuant to IFRS or measures readily reconcilable to IFRS. The targets reviewed by management may encompass both non-GAAP measures and non-financial metrics (e.g., those related to ESG objectives, such as greenhouse gas (GHG) emissions). Incorporating the actual performance on these non-financial or non-GAAP measures into financial statement disclosures would subject them to reasonable assurance, and therefore require the development of additional processes and controls, increasing the cost of providing such non-financial and non-GAAP disclosures relative to other materials in which an entity would more typically publish them (such as investor relations materials). In addition, the inclusion of non-GAAP measures may also create additional disclosure requirements under securities regulation.

In addition, if these requirements are retained, we suggest that the Board consider leveraging this disclosure to reduce the burden of impairment testing. In particular, we recommend that a full impairment test not be required for goodwill arising in business combinations, whether strategic or not, in the annual reporting period in which the acquisition occurs, and that an entity instead be permitted to perform an assessment for indicators of impairment. In the absence of a material adverse event, which would be identified through the indicator assessment, performing an annual impairment test in the year of acquisition provides limited value but may involve significant cost and effort for preparers to develop

appropriate models and processes while also preparing the acquisition-date disclosures. For strategic business combinations, users would be able to look to the additional disclosures, while for other acquisitions the cost savings of not performing the testing would outweigh any informational benefits of a full impairment test where there are no indicators of impairment.

Thresholds for disclosure of strategic business combinations (Question #2)

To the extent the disclosure requirements are retained, we agree that they should only apply to a subset of material business combinations, and that those of strategic significance are the appropriate population. We also agree that the use of a threshold approach to define the population is important because many observers believe that most acquisitions are strategic, regardless of size (i.e., in the absence of a threshold, all acquisitions could be captured in the definition of "strategic business combinations").

We recommend that the Board significantly increase the quantitative threshold to better reflect the materiality of a strategic acquisition. Paragraph IFRS 3.BC54, in the Basis for Conclusions, explains that a strategic business combination is to be interpreted as one where the failure to meet any of the entity's acquisition-date key objectives would put the entity at serious risk of failing to achieve its overall business strategy. A threshold of 10% does not appear to be commensurate with this level of potential risk to an entity's overall strategy. We would instead propose a higher threshold, such as 20%, which is within the range of 5% to 30% noted in IFRS 3.BC67 that the Board observed in its research into the thresholds in local regulations. We do not believe that it is necessary to align to the 10% threshold in IFRS 8 given the wide range of quantitative thresholds applied by regulators, with 30% being the Canadian Securities Administrators' (CSA) threshold for "significant acquisitions", which is the trigger for filing additional reporting on the acquired business and the impact of the acquisition on the acquirer in the form of a "Business Acquisition Report" (BAR). This 30% threshold is applied in the income, asset, and investment test, with a BAR required if any two of the three tests are met. Of note, in 2020, following public consultation, the CSA increased this threshold from 20% to 30% for reporting issuers that are not ventures issuers, specifically to address the regulatory burden on reporting issuers.

With respect to the qualitative threshold, we encourage the Board to provide additional application guidance for the assessment of the qualitative threshold in terms of how to identify a major/material new line of business or geographical area. For example, it is unclear if this threshold would capture circumstances such as an entity (i) re-entering a geographical area, (ii) entering a geographical area that has substantially the same legal and operating environment as its existing operations, or (iii) acquiring an entity where the parent company has operations in a region where the acquirer already operates, but that has subsidiaries operating in another region where the acquirer does not have operations.

Disclosure of the information reviewed by an entity's key management personnel (Question #4)

We do not agree that the information reviewed by key management personnel should be the basis for the proposed disclosures for strategic business combinations and recommend that the Board revert to the information reviewed by the chief operating decision maker (CODM), as contemplated in the discussion paper. The CODM would review the material objectives and targets of any strategic acquisitions, and particularly those where the failure to achieve a key objective would put the entity at serious risk of failing to achieve its overall business strategy. Key management personnel will often review additional, immaterial objectives and targets for strategic acquisitions, the disclosure of which may obscure material information, and would require additional judgment by preparers to identify those targets that should be disclosed, whereas the information reviewed by the CODM would generally be the most material objectives and targets.

In addition, irrespective of whether the disclosure is based on information reviewed by key management personnel or the CODM, we do not agree that the information required to be disclosed should be identified exclusively based on the scope of management's review. This would tie external reporting too closely to internal management reporting, including that there could be certain confidential information that would be reviewed internally for management or regulatory reporting purposes that is not meant to

satisfy external reporting obligations. We recommend that additional qualitative factors be introduced to identify the information that should be disclosed, including consideration for the confidentiality and commercial or regulatory (e.g., competition) sensitivity of the information.

We do not agree that an entity should be required to disclose information about the performance of a business combination for as long as it is reviewed by management, as management's reasons for reviewing the information may go beyond its assessment of the success of the acquisition. For example, an acquiree may be set up as a separate legal entity or operating segment, and the information reviewed by management may be the product of normal legal entity or internal management reporting rather than targeted reporting to review the status of the acquisition. In addition, different companies may review results for different timeframes, resulting in diversity in practice and placing an ongoing disclosure burden on only certain market participants. We recommend that the disclosures instead be required for the lesser of the period that the CODM reviews the performance and a specified maximum number of annual reporting cycles, such as after the two years during which additional disclosure would be required if the entity stopped reviewing objectives and targets.

Finally, while we generally agree with the proposal to require disclosure that key management personnel have not reviewed the achievement of a key objective and the related targets in a particular period, disclosing this for each acquisition-date key objective and related target appears to be overly detailed, and more focused on a compliance approach than balancing the costs and benefits of disclosure. We therefore recommend that an entity be permitted to provide this disclosure for a group of key objectives related to a particular strategic business combination as a whole, as appropriate in the circumstances, particularly where the rationale for stopping or not starting management's review is the same across the various objectives and targets.

Exemption from Disclosing Information (Question #3)

While we agree in principle with the inclusion of an exemption, it is unclear from the proposed guidance the fact patterns that would be acceptable under B67D(a), and whether the circumstances would be so rare that the exemption would not be usable in practice. In the absence of the removal of the disclosure requirements, we suggest that the exemption criteria be broader, including to exempt the disclosure of information on strategies that deliver a competitive advantage and exempting information whose disclosure would be contrary to antitrust laws and other similar regulations. In its current form we are concerned that the costs of making such disclosures and assessing if the exemption applies would outweigh the incremental benefits.

We also recommend that the exemption permit entities to omit the disclosures in B67A(b)(i), which requires an acquirer to disclose information about the actual performance of the strategic business combination. We suggest that entities instead provide qualitative disclosure on the performance, such as the performance statement specified in B67A(b)(ii). The disclosure of quantitative information on actual performance would appear to be contrary to the intent of the exemption to prevent the disclosure of prejudicial information. As well, disclosing this information without disclosing the key objectives and related targets or a statement of whether the actual performance is meeting management's expectations, would create ambiguity, and lead to speculation and potential misinterpretation of how the actual performance compares to management's objectives.

We support the inclusion of application guidance, however, the proposed guidance is overly restrictive for the reasons noted above. The circumstances that are exempted from disclosure can be difficult to reach or substantiate, and would require significant judgment, which will make the assessment challenging to audit. We recommend that the IASB provide additional application guidance and/or illustrative examples to demonstrate circumstances in which the exemption could be applied. In particular, the criteria for what constitutes a "seriously prejudicial effect" on the achievement of an entity's acquisition-date key objectives are unclear and inherently subjective, and could lead to significant variability in application across different entities, industries or regions.

New disclosure objective (Question #5)

As discussed above, we disagree with the proposed objective of disclosing the benefits an entity expects from a business combination, particularly to the extent it drives quantitative disclosure of these benefits in the form of disclosure on the expected quantitative amount of synergies in the year of acquisition, as proposed in IFRS 3.B64(ea).

Contribution of the acquired business (Question #5)

The Board has proposed to amend the requirement to provide proforma information on the performance of the combined entity from the beginning of the fiscal year to the date of the acquisition, in IFRS 3.B64(q)(ii), to specify that the acquirer will develop an accounting policy to prepare this information and that this policy should result in proforma information that will help users to forecast the future financial performance of the combined entity.

We recommend that the Board reconsider the proposed objective in B64(q)(ii) of helping users to "forecast future performance of the combined entity". This objective would seem to suggest that an entity should not only reflect synergies that might have occurred in the pre-acquisition period, but that it should include further, unspecified assumptions to help predict future performance. We also suggest that the Board clarify that an entity be able to determine the accounting policy used to provide this proforma information for each business combination, since different policies and practices may be required to compile this information depending on the business involved, the nature of the identifiable assets and liabilities acquired, and the availability of historic financial information for the acquired business during the pre-acquisition period.

Additional amendments of disclosure requirements in IFRS 3 (Question #5)

In the ED the Board also proposes other amendments to the disclosure requirements in IFRS 3. We are supportive of these proposals as follows:

- **Disclosing the strategic rationale for a business combination**: The Board proposes to change from the existing requirement to disclose the "primary reasons" for a business combination to a new requirement to disclose the "strategic rationale". We agree with the proposal, as it aligns with the way management typically assesses acquisition targets, and satisfies the information needs of users.
- **Disclosing the classes of assets acquired and liabilities assumed:** The Board proposes to delete the word "major" from the requirement in IFRS 3.B64(i) to disclose the amounts recognized as of the acquisition date for each "major" class of assets acquired and liabilities assumed. The Board also proposed to add defined benefit pension liabilities and financing liabilities to the Illustrative Examples accompanying IFRS 3. We agree with these proposals as the meaning of "major" is not clear and materiality should instead be the deciding factor to determine if a class of assets or liabilities should be separately disclosed.
- **Deleting disclosure requirements**: The Board proposes to delete paragraphs IFRS 3.B64(h) relating to the disclosures for acquired receivables, IFRS 3.B67(d)(iii) that requires disclosing adjustments resulting form the subsequent recognition of deferred tax assets in the continuity of the goodwill carrying value, and IFRS 3.B67(e) that requires disclosure on the amount and an explanation of any gain or loss recognized in the current reporting period relating to the identifiable assets acquired or liabilities assumed. We agree with these proposals, as this will reduce the effort of preparing these disclosures without significantly impacting the quality of information available to users.

<u>**Changes to the IAS 36 Impairment Test**</u>

Proposal to reduce shielding (Question #6)

The Board has arrived at a preliminary view to replace the phrase ‘goodwill is monitored’ in IAS 36.80(a) with ‘business associated with the goodwill is monitored’ to determine the level at which the goodwill acquired in business combinations is allocated to CGUs. This is intended to clarify that an entity is required first to determine the lowest level at which the business associated with the goodwill is monitored for internal management purposes and to help an entity allocate goodwill to a level consistent with how it reports internally and manages its operations.

We disagree with the proposed amendments, as IAS 36.80A(a) does not consider the challenges of applying these amendments once management stops separately tracking the synergies, including for longstanding legacy acquisitions where the data on the original expected synergies is no longer available and where the original acquired business may now be significantly altered or integrated within the entity. Management may also have intended for synergies at a higher level than the business associated with the goodwill. As a result, while some monitoring may occur at the level of the business associated with the goodwill, the more meaningful results would be at a higher level where synergies are produced. The proposals would require entities to potentially restructure their internal reporting mechanisms to align with the new definitions, adding complexity and operational costs. Such change could be costly and overly complicated, while making information less comparable since CGUs would be monitored and reported at different levels for internal and external shareholders.

To the extent that the proposed amendments do proceed, we recommend that the Board provide additional application guidance and illustrative examples to assist preparers in interpreting and applying this guidance. We also recommend that the Board specify that the amended allocation of goodwill to CGUs would only apply as of the first full annual impairment test following the effective date of the amendments. In the absence of this, a change in the CGU allocation could impact the assessment for indicators of impairment in the first interim reporting period after the adoption of the amendments, resulting in an off-cycle impairment test immediately after adoption of the amendments, which would create additional cost for preparers.

Additional Changes to the Impairment Test (Question #6 & 7)

In the ED the Board also proposes other amendments to the impairment test and disclosure requirements in IAS 36. We are supportive of these proposals as follows:

- **Removal of constraint on including cash flows from future restructuring**: The Board proposes to remove the constraint on including cash flows arising from a future restructuring or improving or enhancing an asset’s performance when calculating value in use. We agree with the proposal as it would align more closely with management’s internal forecasts and operating plans, which would reduce the cost and complexity of developing the cash flows for impairment testing purposes. In addition, the proposal would align the value-in-use approach more closely to the fair value less costs of disposal approach, under which these cash flows may already be included if they would be considered by a market participant in their assessment of fair value.
- **Removal of requirement to use pre-tax cash flows and pre-tax discount rates:** The Board proposes to remove the requirement to use pre-tax cash flows and pre-tax discount rates in calculating value in use, and instead requires an entity to use internally consistent assumptions for cash flows and discount rates. We agree with the proposal since using after-tax inputs would align more closely with how valuations are performed in practice.
- **Reducing management over-optimism:** We agree with the Board’s proposal to disclose the reportable segment in which a CGU or group of CGUs containing goodwill is included.

Goodwill Amortization

We recommend that the Board reconsider reintroducing the amortization of goodwill. This would significantly reduce the cost and subjectivity of impairment testing and mitigate concerns that impairment losses on goodwill may not be recognized on a timely basis, including due to shielding or management over-optimism. While amortizing goodwill may result in the amortization expense being added back to

entities' non-GAAP measures, impairment losses may already be treated as adjusting items under the impairment-only model.

Transition (Question #9)

We agree with the Board's proposal to apply the amendments to IFRS 3 and IAS 36 prospectively from the effective date without restating comparative information, as this is a more relevant and practical way of implementing these requirements.

In addition, as discussed above, to the extent that the proposed amendments to IAS 36.80-83 proceed, we recommend that the Board specify that the amended allocation of goodwill to CGUs would only apply as of the first full annual impairment test following the effective date of the amendments.

Thank you for considering our comments. We would be pleased to discuss our response at your convenience.

Sincerely,