

July 14, 2024

IFRS Foundation
7 West ferry Circus
Canary Wharf
London E14 4HD, United Kingdom

RE: Business Combinations—Disclosures, Goodwill and Impairment; Proposed amendments to IFRS 3 and IAS 36

Dear Colleagues,

The Saudi Organization for Chartered and Professional Accountants (SOCPA) appreciates the efforts of the IASB and welcomes the opportunity to comment on the Exposure Draft, *Business Combinations—Disclosures, Goodwill and Impairment; Proposed amendments to IFRS 3 and IAS 36*.

Our detailed comments on the questions raised in the Exposure Draft are attached in the appendix to this letter.

Please feel free to contact Dr. Abdulrahman Alrazeen at (razeena@socpa.org.sa) for any clarification or further information.

Sincerely,

Dr. Ahmad Almeghames

SOCPA Chief Executive Officer



Appendix: SOCPA Comments on: Business Combinations—Disclosures, Goodwill and Impairment; Proposed amendments to IFRS 3 and IAS 36

Question 1 —Disclosures: Performance of a business combination (proposed paragraphs B67A–B67G of IFRS 3)

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

SOCPA Comments:

SOCPA agrees with IASB’s proposal to require entities to disclose information about the performance of strategic business combinations, subject to an exemption as it seems reasonable and aligned with the objective of providing users with better information about these transactions. However, SOCPA has highlighted some concerns regarding the exemption in the response to question 3 below.

SOCPA believes the proposal strikes a reasonable balance between the benefits of enhanced disclosure and the potential costs and risks associated with disclosing sensitive strategic information. By focusing only on strategic business combinations, the proposal would provide users with valuable insights while mitigating concerns raised by preparers regarding the cost of disclosure.

Question 2—Disclosures: Strategic business combinations (proposed paragraph B67C of IFRS 3)

The IASB is proposing to require an entity to disclose information about the performance of a business combination (that is, information about the entity’s acquisition-date key objectives and related targets for the business combination and whether these key objectives and related targets are being met) for only strategic business combinations—a subset of material business combinations. A strategic business combination would be one for which failure to meet any one of an entity’s acquisition-date key objectives would put the entity at serious risk of failing to achieve its overall business strategy.

The IASB is proposing that entities identify a strategic business combination using a set of thresholds in IFRS 3—a business combination that met any one of these thresholds would be considered a strategic business combination (threshold approach) (see paragraphs BC56–BC73).

The IASB based its proposed thresholds on other requirements in IFRS Accounting Standards and the thresholds regulators use to identify particularly important transactions for which an entity is required to take additional steps such as providing more information or holding a shareholder vote. The proposed thresholds are both quantitative (see paragraphs BC63–BC67) and qualitative (see paragraphs BC68–BC70).

- (a) Do you agree with the proposal to use a threshold approach? Why or why not? If you disagree with the proposal, what approach would you suggest and why?
- (b) If you agree with the proposal to use a threshold approach, do you agree with the proposed thresholds? Why or why not? If not, what thresholds would you suggest and why?

SOCPA Comments:

- (a) SOCPA agrees with the proposal to use a threshold approach to identify strategic business combinations as it seems logical and practical. SOCPA believes this approach provides

clear criteria for entities to determine which combinations warrant additional disclosure, thereby reducing ambiguity and promoting consistency in reporting practices.

SOCPA agrees the closed-list approach, as proposed by the IASB, offers several advantages over an open-list approach since the closed-list approach requires less judgement and avoid difficulties to audit and enforce. SOCPA notes that the closed list approach could capture business combinations that are not considered to be strategic by the management and not capture strategic business combinations that meet the thresholds. Accordingly, we suggest the IASB consider our suggestions made below in fine tuning the closed list approach. It provides clarity and certainty to entities regarding their disclosure obligations, aligns with existing regulatory practices, and facilitates comparability across different entities and industries and therefore reduce implementation costs. However, SOCPA believes the single qualitative threshold which is proposed is very limited. The proposal only requires a business combination that results in the acquirer entering a new major line of business or geographical area of operations to be considered as a qualitative threshold. SOCPA believes this can be extended by including other aspects as well, for example: acquiring a key technology or talent, could be equally strategic but not captured by these thresholds. Therefore, SOCPA suggests the qualitative thresholds be extended to include other aspects to identify “strategic” acquisitions together with a caveat for immaterial business combinations. This matter could be further elaborated in the Basis for Conclusions on the ED.

While the IASB states that the rationale behind the percentages proposed are based on feedback from stakeholders, SOCPA believes the thresholds are somewhat arbitrary. Example: the proposed 10% threshold for quantitative measures (revenue, total assets, operating profit) might be too high or low depending on the specific industry or entity. Therefore, they may not effectively capture the substance of the exposure draft’s objective. Hence, SOCPA suggests that the exposure draft language be amended to state that the thresholds given are to be used as a guide and a lower percentage maybe used based on management judgement, if they believe the industry in which the subsidiary operates warrants a lower percentage when determining quantitative measures. Such language would also allow applying a more principles-based approach in contrast to the rules-based approach i.e. – closed list approach for providing the required information while not distorting the closed-list approach.

Question 3—Disclosures: Exemption from disclosing information (proposed paragraphs B67D–B67G of IFRS 3)

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

SOCPA Comments:

- (a) SOCPA believes the proposed exemption principle could be challenging to apply consistently across different business combinations and may lead to subjective judgments by preparers. Prejudice to the achievement of acquisition-date key objectives is a complex determination influenced by various factors, such as competitive landscape, legal obligations, and market conditions. Without clear guidelines, there's a risk that entities may exploit the exemption to withhold information that could be relevant to users.

To address this concern, the IASB could consider providing more specific criteria or examples illustrating scenarios where the exemption would be appropriate to support preparers in appropriately applying the exemption. Further, examples could demonstrate how entities could disclose the fact that they applied the exemption and information that was previously exempted. This could include defining thresholds or parameters for what constitutes "serious prejudice" and offering guidance on how to assess the likelihood and magnitude of such prejudice.

- (b) SOCPA believes while the proposed application guidance outlines factors for consideration, it may not sufficiently guide entities in assessing the appropriateness of the exemption. The guidance focuses on the effect of disclosing information and the public availability of information, which may not comprehensively cover all relevant considerations.

To enhance the effectiveness of the guidance, the IASB could expand the list of factors and provide more specific instructions on how to weigh these factors in the decision-making process. This could include considerations such as the nature of the information, its materiality, the potential impact on stakeholders, and the feasibility of alternative disclosure methods. Moreover, offering illustrative examples or case studies could help entities better understand how to apply the guidance in practice.

Question 4—Disclosures: Identifying information to be disclosed (proposed paragraphs B67A–B67B of IFRS 3)

The IASB is proposing to require an entity to disclose information about the performance of the entity's strategic business combinations (that is, information about its acquisition-date key objectives and related targets for a strategic business combination and whether these key objectives and related targets are being met) that is reviewed by its key management personnel (see paragraphs BC110–BC114).

The IASB's proposals would require an entity to disclose this information for as long as the entity's key management personnel review the performance of the business combination (see paragraphs BC115–BC120).

The IASB is also proposing (see paragraphs BC121–BC130) that if an entity's key management personnel:

- do not start reviewing, and do not plan to review, whether an acquisition-date key objective and the related targets for a business combination are met, the entity would be required to disclose that fact and the reasons for not doing so;
- stop reviewing whether an acquisition-date key objective and the related targets for a business combination are met before the end of the second annual reporting period after the year of acquisition, the entity would be required to disclose that fact and the reasons it stopped doing so; and
- have stopped reviewing whether an acquisition-date key objective and the related targets for a business combination are met but still receive information about the metric that was originally used to measure the achievement of that key objective and the related targets, the entity would be required to disclose information about the metric during the period up to the end of the second annual reporting period after the year of acquisition.

(a) Do you agree that the information an entity should be required to disclose should be the information reviewed by the entity's key management personnel? Why or why not? If not, how do you suggest an entity be required to identify the information to be disclosed about the performance of a strategic business combination?

(b) Do you agree that:

- (i) an entity should be required to disclose information about the performance of a business combination for as long as the entity's key management personnel review that information? Why or why not?
- (ii) an entity should be required to disclose the information specified by the proposals when the entity's key management personnel do not start or stop reviewing the achievement of a key objective and the related targets for a strategic business combination within a particular time period? Why or why not?

SOCPA Comments:

(a) SOCPA agrees the information an entity should be required to disclose should be the information reviewed by the entity's key management personnel as disclosing information reviewed by KMP ensures that the disclosed information is relevant and useful to stakeholders. KMP are likely to focus on the most critical aspects of business performance, ensuring that users receive insightful and significant data regarding the success and integration of business combinations.

(b)

(i) SOCPA agrees continuous disclosure should be required while KMP review the performance of a business combination as it allows users to assess the effectiveness of

management's decisions and their stewardship of the entity's resources over time. This ongoing review provides a more comprehensive picture of the business combination's impact.

- (ii) SOCPA agrees with this proposal as disclosing that KMP do not start or stop reviewing the achievement of key objectives within a specified time frame provides critical information to users. It informs them of any shifts in management focus and the potential implications for the business combination's success and strategic importance.

Question 5—Disclosures: Other proposals

The IASB is proposing other amendments to the disclosure requirements in IFRS 3. These proposals relate to:

New disclosure objectives (proposed paragraph 62A of IFRS 3)

The IASB proposes to add new disclosure objectives in proposed paragraph 62A of IFRS 3 (see paragraphs Basis for Conclusions (BC) BC 23–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?

SOCPA Comments:

SOCPA disagrees with certain proposed amendments to IFRS 3, as we believe they do not adequately address the fundamental concerns identified during the post-implementation review (PIR) of IFRS 3. While the amendments aim to enhance disclosure and provide users with better information, they fall short in several key areas:

- Proposed paragraph 62A of IFRS 3: The addition of new disclosure objectives aims to provide more meaningful information, but there is a risk that entities may continue to treat these requirements as a checklist. This could result in boilerplate disclosures that fail to provide the intended insights, as entities may focus more on compliance than on the substance of the information provided. Therefore, we think there should be a caveat after paragraph B67C to note that the paragraphs B64 and B67C do not provide an exhaustive list of all potential disclosures that entities could report when complying with the requirements of paragraph 62A.
- Paragraph B64(d) of IFRS 3: The broad and somewhat vague requirement to disclose the "strategic rationale" for a business combination may also result in generic statements that do not significantly enhance user understanding. The IASB should clarify and illustrate how the replacement of term 'primary reasons' with 'strategic rationale' would differ from the current practice.
- Proposed paragraph B64(ea) of IFRS 3:
 - while users expressed a need for better information to assess business combinations, the proposed disclosures might not fully meet these needs. For example, the requirement to disclose the nature, timing, and amount of expected synergies assumes that entities can accurately predict these factors, which may not always be feasible.

- SOCPA understands that each business combination has its unique set of expected synergies which makes it difficult to have a defined term. However, entities might face practical challenges in applying the term 'synergies' in the context of quantifying its impact. The IASB's decision not to provide a definition of "expected synergies" might lead to diverse interpretations and reduce comparability across entities. This can result in varied and potentially misleading information for users.

Question 6—Changes to the impairment test (paragraphs 80–81, 83, 85 and 134(a) of IAS 36)

During the PIR of IFRS 3, the IASB heard concerns that the impairment test of cash generating units containing goodwill results in impairment losses sometimes being recognised too late.

Two of the reasons the IASB identified (see paragraphs BC188–BC189) for these concerns were:

- shielding; and
- management over-optimism.

The IASB is proposing amendments to IAS 36 that could mitigate these reasons (see paragraphs BC192–BC193).

Proposals to reduce shielding

The IASB considered developing a different impairment test that would be significantly more effective at a reasonable cost but concluded that doing so would not be feasible (see paragraphs BC190–BC191).

Instead, the IASB is proposing changes to the impairment test (see paragraphs 80–81, 83 and 85 of IAS 36) to reduce shielding by clarifying how to allocate goodwill to cash generating units (see paragraphs BC194–BC201).

Proposal to reduce management over-optimism

The IASB's view is that management over-optimism is, in part, better dealt with by enforcers and auditors than by amending IAS 36. Nonetheless, the IASB is proposing to amend IAS 36 to require an entity to disclose in which reportable segment a cash generating unit or group of cash-generating units containing goodwill is included (see paragraph 134(a) of IAS 36). The IASB expects this information to provide users with better information about the assumptions used in the impairment test and therefore allow users to better assess whether an entity's assumptions are over-optimistic (see paragraph BC202).

(a) Do you agree with the proposals to reduce shielding? Why or why not?

(b) Do you agree with the proposal to reduce management over-optimism? Why or why not?

SOCPA Comments:

- (a) While SOCPA agrees with the proposals to reduce shielding, it believes that some limitations exist. The proposals focus on improving the application of existing rules, which may not entirely eliminate shielding. SOCPA believes paragraph 80A(b) of IAS 36 needs to be redrafted because it introduces a requirement that seems to be a further requirement to the requirement in paragraph 80(a). The last sentence of paragraph 80A(b) requires financial information to reflect how the benefits expected from the synergies of the combination are managed, whereas paragraph 80(a) and the introduction in paragraph 80A(b) only focus on the monitoring of the business by the management. Such conflict could result in shielding if the financial information in paragraph 80A(b) is applied in its entirety. Therefore, SOCPA recommends removing the last part of paragraph 80A(b). Such redrafting would also make it consistent with paragraph 83(b) of IAS 36. Basis for conclusions paragraph BC197 highlights a concern that entities might be allocating goodwill to operating segments by default, not necessarily reflecting how management monitors the business associated with the goodwill. SOCPA believes this is a potential misalignment between the allocation level and the actual level of management oversight. The proposed changes aim to address this by requiring entities to first identify the level where management monitors the business. However, entities might still be able to define "internal monitoring" at a higher level than where the business is truly managed. This could create some headroom for impairment absorption.
- (b) SOCPA agrees with the proposal to reduce management over-optimism as it assists in meeting the project objectives.

Question 7—Changes to the impairment test: Value in use (paragraphs 33, 44–51, 55, 130(g), 134(d)(v) and A20 of IAS 36)

The IASB is proposing to amend how an entity calculates an asset's value in use. In particular, the IASB proposes:

- to remove a constraint on cash flows used to calculate value in use. An entity would no longer be prohibited from including cash flows arising from a future restructuring to which the entity is not yet committed or cash flows arising from improving or enhancing an asset's performance (see paragraphs BC204–BC214).
- to remove the requirement to use pre-tax cash flows and pre-tax discount rates in calculating value in use. Instead, an entity would be required to use internally consistent assumptions for cash flows and discount rates (see paragraphs BC215–BC222).

- (a) Do you agree with the proposal to remove the constraint on including cash flows arising from a future restructuring to which the entity is not yet committed or from improving or enhancing an asset's performance? Why or why not?

- (b) Do you agree with the proposal to remove the requirement to use pre-tax cash flows and pre-tax discount rates in calculating value in use? Why or why not?

SOCPA Comments:

- (a) SOCPA believes allowing future cash flows from restructuring and enhancements could lead to overly optimistic projections by management, potentially delaying the recognition of impairment losses. Without additional constraints, there is a risk that the impairment test could be manipulated to avoid recognizing impairments, reducing the reliability of the financial statements. Additionally, including cash flows from future restructuring and enhancements may conflict with the principle of measuring the value in use of an asset in its current condition. This approach could indirectly allow the recognition of internally generated goodwill, which contradicts the existing prohibition on recognizing such goodwill and result in difficulties to audit and enforce and hence higher costs.
- (b) SOCPA agrees with the proposal of removing the requirement to use pre-tax cash flows and discount rates as it simplifies the impairment testing process and aligns it with common valuation practices, which typically use post-tax cash flows and discount rates. This change will reduce the burden on entities to calculate pre-tax rates, which are not commonly used in practice.

Question 8—Proposed amendments to IFRS X Subsidiaries without Public Accountability: Disclosures

The IASB proposes to amend the forthcoming IFRS X Subsidiaries without Public Accountability: Disclosures (Subsidiaries Standard) to require eligible subsidiaries applying the Subsidiaries Standard to disclose:

- information about the strategic rationale for a business combination (proposed paragraph 36(ca) of the Subsidiaries Standard);
- quantitative information about expected synergies, subject to an exemption in specific circumstances (proposed paragraphs 36(da) and 36A of the Subsidiaries Standard);
- information about the contribution of the acquired business (proposed paragraph 36(j) of the Subsidiaries Standard); and
- information about whether the discount rate used in calculating value in use is pre-tax or post-tax (paragraph 193 of the Subsidiaries Standard).

See paragraphs BC252–BC256.

Do you agree with the proposals? Why or why not?

SOCPA Comments:

SOCPA agrees that disclosing the strategic rationale provides users with valuable context, helping them understand the purpose and expected benefits of the business combination.

However, preparing this disclosure might be challenging for subsidiaries with limited resources, as it requires articulating strategic objectives clearly.

SOCPA believes providing quantitative information about expected synergies helps users assess the anticipated benefits and the financial logic behind the business combination. However, this requirement might be burdensome for subsidiaries, particularly if the synergies are complex or if the data is not readily available.

SOCPA agrees that information about the acquired business's contribution would allow users to evaluate its performance and its impact on the subsidiary's financials.

SOCPA also agrees that disclosing whether the discount rate is pre-tax or post-tax enhances the transparency in calculating value in use. It would help users understand the assumptions underlying the valuation and the associated uncertainties.

Question 9—Transition (proposed paragraph 64R of IFRS 3, proposed paragraph 1400 of IAS 36 and proposed paragraph B2 of the Subsidiaries Standard)

The IASB is proposing to require an entity to apply the amendments to IFRS 3, IAS 36 and the Subsidiaries Standard prospectively from the effective date without restating comparative information. The IASB is proposing no specific relief for first-time adopters. See paragraphs BC257–BC263.

Do you agree with the proposals? Why or why not? If you disagree with the proposals, please explain what you would suggest instead and why.

SOCPA Comments:

SOCPA believes applying the amendments prospectively avoids the significant practical challenges and costs associated with gathering historical data to restate past periods. Historical data may not be readily available or may require considerable effort to reconstruct accurately, which could impose undue burdens on entities.

SOCPA also suggests that the revised standard offers targeted relief measures for first-time adopters, particularly regarding the performance review of past business combinations. This could involve limited exemptions for certain disclosures, reducing the initial compliance burden.