



Hong Kong Institute of
Certified Public Accountants
香港會計師公會

Meeting with SMPC Technical Issues Working Group
(via videoconference)

Date: 22 September 2020, Tuesday
Time: 3:00 p.m. – 5:00 p.m.

Members Present: Gary Poon, Poon & Co.
Kenneth Lau, Crowe (HK) CPA Limited
Chan Lok Sang, Lau & Au Yeung C.P.A. Limited
Colin Chau, RSM Hong Kong
Sammy Choi, TKC Corporate CPA Limited
Philip Fung, Lak & Associates CPA Limited
Anntice Lai, D & Partners CPA Limited
Frank Lam, BDO Limited
Elizabeth Law, Law & Partners CPA Limited
Thomas Wong, Nexia Charles Mar Fan & Co.
Jimmy Yip, Mazars CPA Limited
Sharon Chan, Grant Thornton Hong Kong Limited
Basilia Wong, HLB Hodgson Impey Cheng Limited

Staff in attendance: Tiernan Ketchum, Associate Director, Standard Setting, HKICPA
Norman Chan, Associate Director, Standard Setting, HKICPA
Joni Kan, Associate Director, Standard Setting, HKICPA

Apologies: Webster Ng, Webster Ng & Co.
Wing Chan, BDO Limited

IASB Discussion Paper DP/2020/1 *Business Combinations – Disclosures, Goodwill and Impairment*

1. Improving disclosures about acquisitions

Proposed disclosures

- One member supported the proposed new disclosure requirements and considered that the proposal is reasonable and logical.
- Some members raised concerns on the proposed new disclosures, including:
 - One member noted that focusing on disclosures may not address the fundamental problems arising from the current impairment-only approach for the subsequent accounting of goodwill. This member recommended the IASB better considers the root accounting cause of the problems, and reconsiders whether additional disclosures should be introduced to address those problems. For example, the IASB should consider what goodwill represents and determine its accounting according to its nature. Another member echoed in this member's view that the proposed new disclosures could not address the underlying issue. This later member observed that many investors are interested in the overall performance of the group, e.g. share price of the company, but not the performance of individual acquisitions, and considered the proposed new disclosures could not provide useful information to investors.
 - One member shared his view that there are many disclosure requirements under IFRS 3 *Business Combinations* and IFRS 8 *Operating Segments*, which already provide sufficient information to investors regarding the acquisitions

and the subsequent performance of the acquiree. The member also noted the disclosure requirements under IFRS 12 *Disclosure of Interests in Other Entities* do not require specific disclosures for material subsidiaries. This member questioned why additional disclosures are required for acquisitions (i.e. acquisition of subsidiaries) as significant time and costs are involved for preparers to comply with such proposed requirements. Furthermore, limited useful information is provided to investors, as they would be more interested in the performance of the group, rather than individual acquisitions. Nonetheless, this member agreed the objectives of acquisitions should be disclosed in the financial statements.

- One member shared her concerns that the proposed new disclosure requirements are qualitative in nature and this would result in increased audit difficulties. In addition, this member considered that because of the qualitative nature of the disclosures and the fact that they are not based on historical financial information, that such disclosures should be made outside the financial statements, e.g. director's report, business review or management commentary¹. Furthermore, this member considered that for companies that are active in acquisitions, for example, a company may have a number of transactions in a year and accumulate hundreds of acquisitions over the years. If disclosures are required for each acquisition, the volume of disclosures would be huge and continuously disclosing this information would be burdensome. Another member also shared the same concern and considered such continued disclosures related to all acquisitions would not be helpful to the investors².

Proposed basis for disclosures and commercial sensitivities

- One member supported the IASB's approach for the proposed disclosures to make analogy to the management approach used for segment reporting under IFRS 8 because going beyond this level may be costly to perform and lead to excessive disclosures. This member considered that further information could be disclosed as a supplement, if necessary, if that additional information is relevant to an understanding of the financial statements that is not presented elsewhere as required by paragraph 112 of IAS 1 *Presentation of Financial Statements*.
- Some members did not agree with the IASB's approach. One member raised a concern that the chief operating decision maker (CODM) may have the power to consider what information to be disclosed in the financial statements and this could increase the challenges for auditing purposes. For example, it is difficult for auditors to assess whether the CODM is a reasonable person to make such a decision as, for example, not to monitor a significant acquisition and thus not to disclose the related information in the financial statements. This member suggested the IASB to provide guidance on how to perform such assessment.
- Another member questioned whether the proposed disclosures based on information reviewed by the CODM would be sufficient, as the CODM monitors the performance of the whole company by segment, while the acquisition is normally carried out at a lower level (i.e. subsidiary level).
- One member commented that there could be diversity in interpretation of "commercial sensitivity" in practice and this could encourage companies to use it as an excuse not to disclose the CODM's objectives for an acquisition and metrics used to monitor whether those objectives are being met. This member agreed that commercial sensitivity is not a valid reason for companies not to disclose useful and relevant information, given investors have a right to know such information, and suggested the

¹ Paragraph 2.32 of the DP explains that the IASB takes the view that all companies should provide the information on the same terms. Not all companies produce a management commentary and not all management commentaries may be available to investors on the same terms as the financial statements. The IASB's preliminary view is that companies should be required to disclose information about strategic rationale, objectives and related targets in the financial statements.

² Paragraphs 2.15-2.16 of the DP explain that the IASB's preliminary view is that companies should disclose information management (CODM) uses internally to monitor acquisitions, and also disclose the fact if management does not monitor an acquisition.

IASB should define “commercial sensitivity” and provide application guidance on how to consider whether information disclosed is commercially sensitive (if it considers to pursue this proposal).

Constraints on proposed disclosures

- Two members commented that information related to the objectives of the acquisitions along with the detailed targets is necessarily forward-looking information, given forward-looking assumptions are used to estimate the future cash flows and quantify the expected synergies arising from the acquisitions. As such, they disagreed with the notion in the DP that such information was not “forward-looking”.

Disclosure objectives and other improvements to IFRS 3 disclosures

- One member supported the IASB’s preliminary view to add specific disclosure objectives and other improvements to IFRS 3 disclosures. However, this member commented that requiring companies to include the proposed disclosures around expected synergies in the year of acquisition would increase the difficulties for verifications by auditors. This is because not all companies would quantify the expected synergies at the acquisition date and companies may be required to estimate such amounts only for disclosure purpose.

2. Goodwill impairment and amortisation

Effectiveness of impairment test and amortisation of goodwill

- Those members who commented on these questions expressed a preference for amortisation, both from a conceptual and practical perspective.
- One member commented that it would be better to first consider what goodwill is, what it represents and what is its nature, before discussing proposed disclosures or its subsequent accounting. This member noted that the DP appears to overly focus on a disclosure-based solution rather than the accounting for goodwill.
- One member commented that goodwill is static and that after an acquiree is integrated it becomes challenging to separately track and distinguish that acquiree.
- One member commented that amortisation will help show the consumption of goodwill, which may at acquisition date represent future expected cash flows from an acquiree. This member commented goodwill can be analogized to a prepayment, and that amortisation with an appropriate period could hence represent the payback period.
- A couple of members commented that the impairment test is highly subjective and hence allows for significant management discretion in its application. One member noted that there additionally may be strong management incentives to avoid impairment (or any other form of cost allocation of goodwill such as amortisation). One member commented that a more effective method of impairing goodwill is to apply amortisation.

3. Other topics

Removal of annual impairment test and Simplification of value in use

- A member commented that removal of the annual impairment test may increase the chance of manipulation of the goodwill impairment mechanism by management as the impairment testing process may become less robust.

Presentation of total equity excluding goodwill

- A couple of members commented that stakeholders are able to easily compute the proposed amount. As such, they found the proposal unnecessary and in general

disagreed with presenting total equity excluding goodwill. They also noted the proposal calls into question why goodwill is being highlighted as such, and what this implies (e.g. whether it is an asset).

Separate recognition of Intangibles

- One member commented that the current recognition criteria for intangible assets acquired in a business combination is acceptable. This member nevertheless noted that certain intangibles (e.g. brand name, customers list) are often nebulous to value and can be difficult to distinguish from goodwill and rest of the company.