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

<u>Our Ref.: C/FRSC</u>

Sent electronically through the IASB Website (www.ifrs.org)

12 July 2024

Dr Andreas Barckow
International Accounting Standards Board
Columbus Building
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Dear Andreas,

IASB Exposure Draft
Business Combinations—Disclosures, Goodwill and Impairment
(Proposed amendments to IFRS 3 and IAS 36)

The Hong Kong Institute of Certified Public Accountants (HKICPA) is the only body authorised by law to set and promulgate standards relating to financial reporting, auditing, ethics and sustainability disclosures for professional accountants in Hong Kong. We are grateful for the opportunity to provide our comments on this Exposure Draft (ED).

The HKICPA appreciates the IASB's efforts in addressing users' needs for better information about the performance of business combinations, while balancing preparers' concerns about cost and commercial sensitivity through the proposed changes to IFRS 3 *Business Combinations*. The HKICPA also welcomes the IASB's initiative to reduce cost and complexity of the impairment test by proposing targeted improvements to IAS 36 *Impairment of Assets*. However, we have significant concerns about certain aspects of the proposals. We provide detailed comments in the Appendix and summarise our primary concerns and recommendations below.

<u>Proposed amendments to IFRS 3</u>

We agree with the overall direction of the proposed disclosures that they should only be applied to a subset of material business combinations, subject to an exemption. However, we have significant concerns in the following areas:

Scope of strategic business combinations

We see the merits of applying a threshold approach as it is easier to use, audit and enforce. Nevertheless, we are concerned that the proposed thresholds would not effectively capture the intended population of strategic business combinations as described in BC54 of the ED and may capture many more business combinations than what we would consider to be strategic business combinations, for the following reasons:
- The proposed 10% threshold appears too low compared to the local listing rules to provide additional information for significant acquisitions.
- The proposed quantitative thresholds only focus on the size of business combinations in terms of revenue, operating profit or loss and total assets, without considering whether the transactions are of any strategic value to the acquirer. Furthermore, when calculating the thresholds, the acquirer and acquiree's financial information may be distorted e.g. due to significant non-recurring items, making it unrepresentative of the usual state of their financial performance and position.

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- The proposed qualitative threshold is not sufficiently clear on whether it is targeting major and strategically important acquisitions geographically.

We acknowledge the challenges in defining a universal set of thresholds that would accommodate the diverse types of acquisitions and business strategies across entities. Therefore, if the IASB's intention were to capture only sizable business combinations, we recommend the IASB reset the proposed 10% threshold to a higher one to be more in line with capital market regulations for major acquisitions, provide guidance and clarifications to address the identified issues for qualitative and quantitative thresholds, and rename the term 'strategic' to another term, such as 'major' or 'substantial', to reflect the specific criteria that characterise the relevant business combinations.

However, if the IASB's intention were to identify both strategically important and sizable business combinations, we suggest the IASB consider using a principle-based approach with BC54 as the principle and the proposed thresholds as indicators rather than determinative factors for a strategic business combination. Under this approach, entities could rebut the presumption by providing reasonable justifications and additional disclosures.

Disclosure of key objectives, targets and expected synergies

We have identified practical questions relating to the disclosure of key objectives, targets and expected synergies, and recommend the IASB provide guidance or clarification on how the proposals should be applied. These questions include:

- An entity's objectives for an acquisition are often broad and subjective in nature, and there could be difficulties in objectively identifying the key objectives of a strategic business combination. In particular, our respondents considered that potential risk factors adversely impacting the achievement of the key objectives could be an impediment to the success of a business combination and are useful information to users. They questioned whether potential risk factors would warrant disclosure.
- The key objectives of a strategic business combination could be financial-related or non-financial related. In cases where the key objectives of a strategic business combination are to achieve branding, technological and innovation-related benefits, the ED is not clear as to whether, and if so, how entities should set the measurable targets and quantify the expected synergies for non-financial objectives for disclosures.
- There is a lack of clarity on what 'synergies' mean in the ED. Specifically, our preparers and users questioned whether the proposed disclosures intend to capture the revenue of the combining operations or incremental revenue. Without clear explanations, entities would prepare the disclosures on different bases and users may interpret the quantitative information differently.

Exemption from disclosures

The application of the disclosure exemption requires a high level of judgement in identifying circumstances that '*can be expected to prejudice seriously the achievement of any of the acquirer's acquisition-date key objectives for the business combination*'. However, the proposed application guidance does not provide sufficient direction on the specific circumstances where the exemption can be applied. It is also unclear whether the exemption would only apply in '*extremely rare cases*', similar to the exemption in IAS 37 *Provisions, Contingent Liabilities and Contingent Assets.* This lack of clarity leaves significant room for interpretation and subjectivity in restricting the exemption only to the appropriate circumstances.

Given the above, we recommend the IASB provide application guidance and examples of legitimate circumstances that qualify for the disclosure exemption to mitigate a risk of diversity in practice. This recommendation, together with those on the scope of strategic business combinations and disclosures of key objectives, targets and expected synergies explained above, could enhance the overall robustness of the proposals and enable entities to focus on the most important information for the most important business combinations in a cost-efficient manner, while mitigating potential debate between preparers and auditors.

Expectation gap on the level of assurance provided

Our practitioners expressed significant concerns that users and regulators might assume auditors had performed work to provide reasonable assurance of the existence and achievability of key objectives, targets and expected synergies disclosed in audited financial statements, exposing auditors to litigation risk when users rely on that information for decision making and suffer losses. This creates an expectation gap between the assurance provided by auditors and the assurance perceived by users.

To address this, we recommend the IASB clearly specify in the body of IFRS 3 that the key objectives, targets and expected synergies are solely based on information prepared and reviewed by the entity's management and represent management's best estimate at the time of acquisition, and there is no guarantee that the actual results will align with the disclosures. In addition, entities should disclose this management assertion in the financial statements. We believe that this approach would be consistent with paragraph 122 of IFRS 18 *Presentation and Disclosure in Financial Statements,* which requires a company to disclose a statement to set appropriate expectations around the nature and reliability of the information provided, helping users understand the inherent uncertainty and mitigate the expectation gap.

If you have any questions regarding the matters raised in this letter, please contact Kennis Lee (kennislee@hkicpa.org.hk), Associate Director or Sam Chan (samkcchan@hkicpa.org.hk), Manager of the Standard Setting Department.

Sincerely,

Cecilia Kwei

Cecilia Kwei
Director of Standard Setting

<u>Work undertaken by the HKICPA in forming its views:</u>

The HKICPA:
(a) issued an Invitation to Comment on the ED on 15 March 2024 to its members and other stakeholders;
(b) sought input from its Business Combinations and Reporting Entity Advisory Panel, Financial Reporting Valuation Advisory Panel and Small and Medium Practices Committee and its Technical Issues Support Group, which mainly comprise technical and industry experts from large as well as small and medium accounting firms (collectively, Practitioners);
(c) held a public roundtable discussion for local stakeholders, including Practitioners, preparers, valuers and investors on 27 May 2024; and
(d) developed its views through its Financial Reporting Standards Committee, having reflected on its respondents' views. The Committee comprises preparer representatives from various industry sectors, regulators, as well as technical and industry experts from small, medium and large accounting firms.

<u>Detailed comments on the IASB ED</u>

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

1. Our respondents expressed mixed views regarding the proposals of requiring entities to disclose information on the performance of a strategic business combination, subject to exemption. Some respondents, including users of financial statements, supported the proposals as they provide them with useful information about material acquisitions and their subsequent performance. However, other respondents had the following comments.

A. <u>Operational challenges</u>

2. Some preparers raised concerns about the practicability of the proposals. They noted that business strategies and objectives can be intricate and challenging to explain in a simple and easily understandable manner. This creates a burden for entities in determining the *acquisition-date <u>key</u> objectives and the related targets* that are '*<u>critical</u> to the success of the business combination*'. They also questioned the boundaries of key objectives and targets, such as whether potential risk factors adversely impacting the achievement of the key objectives should be disclosed and what the appropriate target would be for this type of non-financial objective. These risk factors could be an impediment to the success of a business combination and are useful information to users. These respondents were concerned that entities would need to devote significant effort and costs to identify and support the key objectives and targets to auditors' satisfaction.

3. Similarly, some practitioners from large accounting firms expressed significant concerns on how the proposals would work operationally. Without precise explanation and clear guidance, they foresaw difficulties for preparers and auditors in objectively determining what the key objectives and targets are and what qualifies for the disclosure exemption (see details of our respondents' comments in paragraph 26). This could cause ongoing debate and inconsistent application across entities, and ultimately undermine the intended objective of the proposals.

B. Usefulness of the information

4. Some respondents questioned the usefulness of the proposed disclosures, noting that existing goodwill impairment requirements already provide certain information regarding the performance of business combinations. The proposed additional disclosures might lead to information overload for users and potentially obscure the most important information of the business combinations. In particular, the proposed thresholds would likely capture many more business combinations than what we would consider to be strategic business combinations (see details of our respondents' comments in paragraphs 15, 16 and 19).

5. There are also concerns about the potential for management bias to influence the disclosures, as entities may have incentives to set objectives and goals that are less ambitious but easier to achieve. Since the reporting entity ultimately decides what would be disclosed in the financial statements, there are doubts about whether the proposed disclosures are unbiased and could capture the most important information of a strategic business combination for the benefit of users.

6. In Hong Kong, small and medium-sized entities (SMEs) often prepare their financial statements using HKFRS (equivalent to IFRS Accounting Standards). These SMEs are usually owner-managed businesses with a limited number of users, and the financial statement users rarely require the information about the performance of business combinations. Furthermore, the cost of preparing and disclosing the information could be significant and would impose a substantial burden on SMEs with limited resources, considering the extent of disclosures for a single transaction and the potential never-ending core time period for disclosing the subsequent performance. Hence, the cost to SMEs preparers outweighs the benefit for users.

C. Auditability of the proposed disclosures

7. Some practitioners expressed significant concerns about the auditability of the proposed disclosures relating to the key objectives, targets and expected synergies from business combinations, given that these disclosures involve forward-looking information which could not be reliably verified by auditors. Some of them also opined that the information should be included in management commentary rather than financial statements for similar reasons stated in BC133 of the ED.

8. Other practitioners from a large accounting firm expressed the view that the auditors could verify whether the disclosed information is consistent with the entity's internal planning documents such as management budgets or forecasts reviewed by the key management personnel, which is similar to the IASB's expectations as described in BC145 of the ED.

9. Nevertheless, these practitioners were concerned about the expectation gap these proposed disclosures could create. Investors and regulators might assume auditors had performed work to provide reasonable assurance of the existence and achievability of the disclosed information when it is included in audited financial statements. There is a risk that users would rely on that information for making decisions and suffer a loss when an entity fails to meet its objectives and targets, exposing auditors to litigation risk.

10. To bridge the expectation gap, these respondents recommended the IASB clearly specify in the body of IFRS 3 that the key objectives, targets and expected synergies are solely based on information prepared and reviewed by the entity's management after due and careful consideration, and represent management's best estimate at

the time of acquisition, and there is no guarantee that the actual results will align with the disclosures.

11. These respondents further recommended that the proposed disclosures should be made in a clear and understandable manner in financial statements, faithfully representing their characteristics to avoid misleading users. To do so, entities are suggested to disclose a statement saying that the key objectives, targets and expected synergies merely provide management's view of an aspect of the performance of business combinations at the time of the acquisition, without asserting certainty or achievability. This approach would be consistent with paragraph 122 of IFRS 18 *Presentation and Disclosure in Financial Statements* when entities use *management-defined performance measures* to communicate to investors management's view of an aspect of the financial performance of the entities.

D. <u>Our recommendations</u>

12. We agree with the overall direction of the proposed disclosures that they should only be applied to a subset of material business combinations, subject to an exemption. We believe that the proposed disclosures would give users more direct and useful information on the performance of business combinations than that provided by the existing goodwill impairment test. We also support requiring entities to provide these disclosures in financial statements instead of management commentary for the reasons stated in BC132-137 of the ED.

13. However, we acknowledge the concerns raised by respondents about the practicability and auditability of the proposals. To make the proposals operational and clear for different stakeholders, we strongly recommend the IASB refine the proposals in the following key areas:

    Key objectives, targets and expected synergies: Given an entity's objectives for an acquisition are often broad and subjective in nature, more precise explanation and guidance from the IASB on the boundaries of key objectives and targets would be helpful for preparers. This includes clarification and guidance on whether potential risk factors would warrant disclosure. In cases where the objective of a business combination is to achieve branding, or technological and innovation-related benefits, we consider more guidance is needed for setting measurable targets as well as a consistent approach to quantify the expected synergies for this type of non-financial objectives for disclosures (see our respondents' comments on paragraph 32 below).

    Scope of strategic business combinations: As the proposed scope seems to cover many more business combinations than what our respondents would expect, the IASB should reconsider the use of a threshold approach and the proposed thresholds (see details of our recommendations in paragraphs 22-24 below). Setting an appropriate threshold would reduce the number of business combinations for disclosures and hence reduce the cost to preparers and the potential information overload to users.

    Exemption from disclosure: The IASB should provide more guidance on commercial sensitivity and the specific circumstances that qualify for the exemption from the disclosure requirements (see details of our recommendations in paragraph 27 below). This could help mitigate the debate between the preparers and auditors.

    Expectation gap on the assurance level: Framing the proposed disclosures from management's perspective, as recommended by our respondents in paragraphs 10 and 11 above, would better align the information with its characteristics and enhance transparency. This would also set appropriate expectations around the nature and reliability of the information provided, helping users understand its inherent uncertainty and mitigate the expectation gap risk between the assurance provided by auditors and the assurance perceived by users.

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

14. A majority of our respondents supported the use of a threshold approach as it is easier to use, audit and enforce. However, they expressed concerns about the appropriateness of the proposed thresholds and questioned whether the threshold approach would effectively capture the intended population of strategic business combinations. Their comments are as follows:

A. <u>Proposed quantitative thresholds</u>

15. Many respondents questioned the appropriateness of the proposed 10% threshold, noting that the local listing rules for additional disclosures apply to acquisitions that meet or exceed the 25% threshold[1]. Without further analysis to justify the 10% threshold (other than referencing the 10% threshold used in IFRS 8 *Operating Segments*), these respondents were not convinced that 10% is the appropriate threshold. They considered the proposed threshold too low and recommended the IASB reconsider the proposals.

16. Some respondents commented that the proposed thresholds may not align with the description of a 'strategic business combination' in BC54 of the ED. BC54 states that a strategic business combination is one *'for which failure to meet any one of an entity's acquisition-date key objectives would put the entity at <u>serious risk</u> of failing to achieve its overall business strategy'*. Applying the quantitative thresholds could, in certain cases, capture business combinations that neither have significant strategic value nor pose serious risk to the acquirer. For example:

    (a) Entity A, a loss-making entity with substantial net assets, acquired a profitable business with minimal net assets. As the acquiree's operating profit exceeds 10% of the absolute amount of Entity A's operating loss, the proposed threshold would classify this as a strategic business combination, regardless of its strategic value or risk to Entity A.

    (b) Entity B acquired a small business with a low net asset value comprising a significant amount of total assets and total liabilities for a relatively small purchase consideration. Since the acquiree's total assets exceed 10% of Entity B's total assets, the proposed threshold would classify this as a strategic business combination, regardless of its strategic value or risk to Entity B.

    (c) Entity C acquired one of its major suppliers, and a substantial portion of the acquiree's revenue is derived from sales to Entity C. Since the acquiree's revenue exceeds 10% of Entity C's revenue, the proposed threshold would classify this as a strategic business combination. However, the post-acquisition sales transactions between Entity C and the acquiree will be eliminated on consolidation. Passing the revenue threshold may not necessarily indicate the

[1] Please refer to Chapter 14.33, Main Board Listing Rules (MBLR) issued by the Stock Exchange of Hong Kong Limited (Hong Kong Stock Exchange) for a summary of the reporting and disclosure obligations for transactions meeting or exceeding 25% threshold, i.e. major acquisitions or very substantial acquisitions as set out in Chapter 14.08.

strategic nature of the acquisition.

17. Some respondents raised questions about the calculation of thresholds in situations where the financial information of the acquirer or acquiree, such as operating profit, is distorted due to significant non-recurring items, resulting in unrepresentative financial information. They noted that Hong Kong listed issuers may be allowed to disregard the calculation or apply an alternative size test with the prior consent of the Hong Kong Stock Exchange in certain situations[2]. These respondents considered that the IASB should provide guidance on how to address this matter, such as whether any adjustment to the financials or an alternative test would be applied in such cases.

18. Our respondents also identified several practical challenges in applying the proposed quantitative test in the ED:

    (a) The acquiree's pre-acquisition financial statements may not be prepared using IFRS Accounting Standards. It would be costly and complex for the acquirer to compile financial information, particularly the operating profit, using IFRS Accounting Standards solely for determining the thresholds.

    (b) The acquiree that prepares IFRS financial statements could have applied different accounting policies than the acquirer, or its reporting period may not coincide with that of the acquirer. As a result, the financial information of the acquirer and acquiree may not be comparable and appropriate for calculating the proposed thresholds. This raises practicability and cost concerns if the accounting policies and reporting period of those financial statements need to be aligned with those of the acquirer.

    (c) The acquirer may face difficulties in obtaining pre-acquisition financial information, especially if it did not conduct formal due diligence due to the nature and size of the business combination.

B. Proposed qualitative thresholds

19. Some respondents commented that the wording in B67C(c) of the ED could be interpreted to capture a business combination that enables the acquirer entering a new geographical area of operation, regardless of the magnitude of that combination and whether it is strategic. For instance, an entity acquired a business that primarily operates in geography A where the entity already has a presence, but the acquiree also has some incidental operations in geography B where the entity does not currently operate and has no plan to expand. Applying the proposed qualitative thresholds would capture this as a strategic business combination as the business combination enables the entity to operate in a new geographical area B. These respondents suggested the IASB clarify whether this is what it intends to achieve and provide more precise description of the qualitative thresholds.

C. Use of a threshold approach

20. A few respondents questioned the appropriateness of using the term 'strategic' to characterise the relevant business combinations using a threshold approach. They commented that whether a business combination constitutes a 'strategic' transaction

[2] Pursuant to [Chapter 14.20](), MBLR, '*Where any calculation of the percentage ratio produces an anomalous result or is inappropriate to the sphere of activity of the listed issuer, the listed issuer may apply to the Exchange to disregard the calculation and/or apply other relevant indicators of size, including industry specific tests*.'

is always determined by management based on an entity's own strategies and this would inevitably be different for different entities. There could be a mismatch in defining a business combination as 'strategic' based on the proposed thresholds, which primarily focus on the size of the business combinations. As the proposal intends to capture a subset of material business combinations, these respondents recommended that the IASB use the descriptions, such as 'substantial' or 'major', to better reflect the scope of additional disclosures in IFRS 3.

21. Given the potential issues associated with the threshold approach, a few respondents suggested adopting a principle-based approach, i.e. using BC54 of the ED as the principle and the proposed thresholds as indicators rather than determinative factors for identifying a strategic business combination. If one of the proposed thresholds is met, an entity could still rebut the presumption by disclosing the fact together with reasonable justifications, enabling the entity to exercise judgement in determining strategic business combinations. However, other respondents expressed concerns that such an approach is subjective and challenging to audit, particularly in determining whether there is a serious risk to the acquirer's overall business strategy.

D. <u>Our recommendations</u>

22. We acknowledge our respondents' concerns that the proposed thresholds may not align with an entity's strategies nor the description for a strategic business combination in BC54 of the ED. We are also aware of the challenges in defining a universal set of thresholds that could accommodate the diverse types of acquisitions and business strategies across entities. In light of these and our respondents' concerns, if the IASB's intention were to capture only major or substantial business combinations, we recommend the IASB improve the threshold approach and proposed thresholds in the following ways:

    (a) Reset the proposed 10% threshold to a higher one to be more in line with capital market regulations for major acquisitions and to capture only sizable business combinations, and provide clear justification for the threshold.

    (b) Provide guidance to address situations where the financials of the acquirer and acquiree are not representative of their usual state of financial performance and/or position and consider whether entities would be allowed to make any necessary adjustments to derive a more appropriate threshold.

    (c) Provide a more precise description of the qualitative threshold to capture only business combinations that represent a major geographic expansion or shift for the entity.

    (d) Rename the proposed term 'strategic' to another term, such as 'major' or 'substantial', to reflect the specific criteria that characterise the relevant business combinations for additional disclosures in IFRS 3.

23. However, if the IASB's intention were to identify both strategically important and sizable business combinations, we suggest the IASB consider our respondents' recommendation to use a principle-based approach, using BC 54 of the ED as the principle, with the proposed thresholds (taking into account our recommendations in paragraph 22(a) to (c) above) serving as indicators rather than determinative factors for a strategic business combination that are rebuttable with reasonable justifications and additional disclosures by entities.

24. While we recognise that the practical challenges mentioned in paragraph 18 above are inevitable, we believe that the above suggested improvements could help entities more effectively identify the intended population of the most important business combinations, and consequently limiting those challenges to a smaller number of business combinations.

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

25. We appreciate the IASB's endeavours to address preparers' concerns about commercial sensitivity and litigation risk by proposing to exempt an entity from disclosing some of the information in specific circumstances. Our respondents are supportive of the disclosure exemption in principle but had the following comments and recommendations.

A. *Specific circumstances for using the exemption*

26. Our respondents considered that the application for the exemption requires a high level of judgement in identifying the circumstances that *can be expected to prejudice seriously the achievement of any of the acquirer's acquisition-date key objectives for the business combination*', as described in B67D of the ED. Nevertheless, the proposed application guidance only prescribes a few circumstances where the exemption is not appropriate but does not provide sufficient guidance on the specific circumstances where the exemption can be applied. This lack of clarity presents significant challenges for both auditors and preparers in objectively assessing and consistently applying the exemption across different companies. In addition, some practitioners are concerned that preparers will have wide latitude to argue that lots of the required information could reasonably be considered prejudicial, potentially rendering the disclosures requirements ineffective. Therefore, our respondents stressed the need for examples to illustrate circumstances where the exemption can be applied.

27. We agree with the respondents' feedback that the proposed application guidance could leave significant room for interpretation and subjectivity in restricting the exemption only to the appropriate circumstances. In addition, it is not clear whether the exemption would be expected to apply only to '*extremely rare cases*', given the IASB's explanation in BC80 of the ED that the principle underpinning the exemption is similar to the approach in IAS 37.92. In light of the above, we strongly recommend the IASB provide more application guidance on commercial sensitivity and the legitimate circumstances and examples where the exemption can be applied. This would help improve the overall robustness of the proposals and mitigate potential debate between auditors and preparers on its appropriate use.

B. *Other concerns*

28. Our respondents noted that the proposal in B67E of the ED allow entities to disclose information at a sufficiently aggregate level so that it would not prejudice seriously the acquisition objectives. However, they questioned whether such aggregated information would still be meaningful and useful for users. They also considered that aggregation may not adequately address their concerns in cases where the entity only engages in one or two business combinations during the reporting periods. Presenting the expected synergies in total for a limited number of business combinations may still be commercially sensitive.

29. We recognise the respondents' comments and consider that the proposed aggregation is not entirely clear. The ED provides an example where an acquirer can aggregate the total amount of expected synergies for each individual business combination without prejudicing seriously any of the acquisition-date key objectives for the business combination (i.e. vertical aggregation). However, the ED is not clear as to whether the acquirer can also aggregate the expected synergies across all their business combinations at a total level (i.e. horizontal aggregation). We consider that the horizontal aggregation approach could not provide useful information to users. As such, we recommend the IASB clarify this in the final amendment.

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

30. We generally agree with the proposals to apply a management approach using the entity's key management personnel for identifying disclosure information for strategic business combinations. This approach allows for the provision of relevant information to users by leveraging information that management already uses internally, thereby minimising the reporting burden on preparers.

31. We note that IFRS 3:B67B(b) includes specific disclosure requirements if the key management personnel stop reviewing the performance of a business combination but continue to receive and monitor it as part of the entity's annual budgeting process for reasons described in BC123 of the ED. We suggest that the IASB reconsider the proposal. Key management personnel would generally be able to access and 'receive' any information on-demand through an ERP or another similar system. Hence it may inadvertently capture situations where the key management personnel is able to access and 'receive' such information, but has not reviewed or monitored it.

Question 5—Disclosures: Other proposals

32. We broadly support the proposals but have some concerns about the practice issues and challenges associated with disclosing the expected synergies from the combining operations in B64(ea) of the ED and recommend that the IASB provide guidance or clarification. These issues include:

    Challenges in quantifying synergies: Our practitioners questioned whether it is possible to reliably quantify expected synergies in all cases. For example, if the synergies arise from increased market share, branding, or technology and innovation, how should an entity measure and quantify the effects? Furthermore, does the entity need to consider the level of reliability and probability of occurrence of the synergies when determining whether to disclose such information?

    Mandatory disclosure despite lack of available data: Our preparers queried whether the disclosure is intended to be mandatory even when the entity does not have the necessary analyses and data on synergies readily available. For example, entities may not break down the synergies by category. This could impose a significant burden on entities to gather information for disclosure.

    Ambiguity around the 'synergies' concept: There is a lack of clarity on what 'synergies' mean in the ED. Specifically, our preparers and users questioned whether the proposed disclosures intend to capture the revenue of the combining operations or incremental revenue. Without clear explanations, entities would prepare the disclosures on different bases and users may interpret the quantitative information differently.

Potential compliance issues for Hong Kong listed entities: Our practitioners were concerned that if entities listed in Hong Kong disclose the expected synergies for the combining operations, such synergy disclosures may constitute a 'profit forecast' under the local listing rules[3]. Depending on the level of detail provided in the disclosure, if the information implicitly quantifies the anticipated level of future profits or losses, it could potentially be treated as a profit forecast and trigger compliance issues for Hong Kong listed entities.

Auditability of synergies: Similar to the comments on question 1, our practitioners questioned whether the information could be reliably auditable, given that it involves future projections.

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

A. *Proposal to reduce shielding*

33. We generally agree with the proposal. We share the IASB's view that the issue of shielding cannot be fully eliminated under the current impairment-only model for goodwill, but that the proposal could still help mitigate shielding and enhance comparability across entities in how they conduct the impairment assessment.

B. *Proposal to reduce management over-optimism*

34. We broadly agree with the proposal as it provides users of financial statements with more useful information, although the proposal does have certain limitations. For example, it cannot reduce management over-optimism in situations where entities do not provide segment information under IFRS 8 or when a reportable segment contains more than one cash-generating unit with goodwill.

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)

A. *Removing the constraint on including uncommitted future restructuring or asset enhancement cash flows*

35. Our respondents expressed mixed views on the proposal. Some respondents agreed with the proposal for reasons similar to BC205 of the ED.

36. However, a few respondents disagreed with the proposal. They considered that the proposal could increase the risk of management over-optimism in calculating value in use (VIU) because management would have more flexibility to include a wide range of assumptions in VIU calculation. This appears to conflict with one of the objectives of the ED to reduce management over-optimism. These respondents also questioned whether auditors could verify cash flows arising from future restructuring to which the entity is not yet committed.

37. Furthermore, some respondents noted the IASB's view in BC213 and BC219 of the ED and considered the VIU measurement would become similar to how fair value is

[3] Pursuant to MBLR Chapter 14.61, a 'profit forecast' means '*any forecast of profits or losses, however worded, and includes any statement which explicitly or implicitly quantifies the anticipated level of future profits or losses, either expressly or by reference to previous profits or loses or any other benchmark or point of reference*'.

determined after applying the proposed changes to the impairment test. Therefore, these respondents questioned whether, and if so, how VIU would differ from fair value going forward.

38. We recognise that the cash flows from uncommitted future restructuring and asset enhancement introduce extra subjectivity and uncertainty into the VIU calculation and could significantly impact the impairment assessment in certain circumstances. Hence, we suggest the IASB add this type of cash flows as an example of key assumptions for disclosure under IAS 36.134(d)(i) & (ii). This would help users better assess the reasonableness of this key assumption and reduce management over-optimism. In addition, we believe that there will remain to be differences between VIU and fair value, as explained in IAS 36.53A, even if the constraint is removed. If the IASB were to proceed with the proposal, we suggest the IASB explain their views in detail in the Basis for Conclusions of the final amendments so as to help entities consider the reasonableness of VIU and fair value when ascertaining the recoverable amount.

B. Removing the requirement to use pre-tax cash flows and pre-tax discount rates in calculating value in use

39. We support the proposal as the post-tax approach aligns with how entities prepare cash flows projections and the valuation practice.

Question 8—Proposed amendments to *IFRS X Subsidiaries without Public Accountability: Disclosures* (Subsidiaries Standard)

40. Some respondents disagreed with adding the proposed quantitative disclosure on expected synergies in the Subsidiaries Standard. Same as the comments on question 5, these respondents anticipated significant challenges in quantifying and auditing the expected synergies disclosures. In addition, subsidiaries without public accountability often have a limited number of financial statements users only, and these users rarely require the proposed information.

41. Considering the cost-benefit of the proposed quantitative information about expected synergies, we suggest the IASB further explore the usefulness of this information for users of private subsidiaries.

Question 9—Transition
(proposed paragraph 64R of IFRS 3, proposed paragraph 140O of IAS 36 and proposed paragraph B2 of the Subsidiaries Standard)

42. We support the prospective application of the proposals because retrospective application is not feasible given the nature of the amendments.

~ End ~