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Subject: DP/2020/1 – ***Business Combinations—Disclosures, Goodwill and Impairment***

The Canadian Securities Administrators Chief Accountants Committee appreciates the opportunity to comment on the International Accounting Standards Board's ("IASB" or the "Board") Discussion Paper *Business Combinations—Disclosures, Goodwill and Impairment* (the "Discussion Paper"). The Canadian Securities Administrators ("CSA") is an organization of Canada's provincial and territorial securities regulators whose objective is to improve, coordinate and harmonize regulation of the Canadian capital markets. The CSA Chief Accountants Committee ("CAC") is comprised of the Chief Accountants from the provinces of British Columbia, Alberta, Ontario and Québec.

We support the IASB's effort to explore whether companies can, at a reasonable cost, provide investors with more useful information about the acquisitions those companies make, and to explore proposals to reduce the cost and complexity of performing impairment tests. We would like to provide the following comments about a few key aspects of the preliminary views outlined in the Discussion Paper that we believe could be further explored.

I. Business Combinations—Disclosures

Question 2(b)(i) – linking strategic rationale to overall business strategy

(a) Paragraph 2.11(a) of the Discussion Paper indicates that the description of the strategic rationale would link the rationale for the acquisition to the company's overall business strategy and that the disclosure of this business strategy is often set out elsewhere in a company's financial reports, for example, in a company's management commentary. In Canada, entities who disclose their overall business strategy do this on a voluntary basis as there is no current regulatory requirement in Canada for this disclosure. We recommend that the Board clarify this description to indicate that a company's strategic rationale for the acquisition be linked to the company's overall business strategy, where the overall business strategy has been disclosed by the entity.

(b) Paragraph 2.11(a) of the Discussion Paper provides the following example of a company's overall business strategy: "*to become the leading company in Region Z*". Absent any information necessary for an investor to understand the nature, timing and risks related to this statement, it may be considered misleading under Canadian securities legislation and we may challenge such statement. We recommend that the Board revise this example.

Question 2(c) – chief operating decision maker

The Board's preliminary view discussed in paragraphs 2.8-2.32 is that it should require disclosures about management's objectives for an acquisition and its subsequent performance using the metrics that management uses to monitor an acquisition's performance and subsequent progress against those metrics. The Board's preliminary view is that this information should be required only for those acquisitions monitored by a company's chief operating decision maker ("CODM"), as described in IFRS 8 *Operating Segments* ("IFRS 8"). While it would appear that basing the disclosure on what the CODM uses to monitor an acquisition may help focus on the most important information about the most important acquisitions, introducing the CODM concept in this context may cause issues similar to those observed with the application of IFRS 8 CODM model, such as the judgements about the components of an entity that are regularly reviewed by the CODM.

Question 2(e) – forward-looking information

The Board's preliminary view, as discussed in paragraphs 2.30 and 2.67, is that the information about the strategic rationale, objectives, related targets and expected synergies for an acquisition is not forward-looking information ("FLI"). Instead, the Board considers the information would reflect management's (i.e. CODM's) target at the time of the acquisition and it would not be a forecast of the expected outcome at the time the company prepares its financial statements. In our view, information about certain metrics for measuring the progress of objectives and targets, including certain synergy information, would be considered FLI, and subject to the requirements in Parts 4A and 4B and section 5.8 of National Instrument 51-102 *Continuous Disclosure Obligations* under Canadian securities legislation. By identifying all acquisition metrics and synergies as non-FLI in the Discussion Paper, there is a risk that the required FLI disclosures under securities legislation may be inadvertently omitted.

Question 4 – synergies

(a) Paragraph 2.91 outlines the Board's preliminary view that it should develop proposals to require a company to disclose: (i) a description of the synergies expected from combining the operations of the acquired business with the company's business; (ii) when the synergies are expected to be realised; (iii) the estimated amount or range of amounts of the synergies; and (iv) the expected cost or range of costs to achieve those synergies. We recommend that the Board clarify that this requirement would only apply where the synergies expected from combining the operations of the acquired business with the company's business are quantifiable.

(b) While the Discussion Paper provides the two examples of synergies from combining operations of the acquiree and the acquirer (i.e., established sales and distribution networks of the acquired business and expected cost savings from future contract negotiations), we recommend that the Board either provide a definition for "synergies", or include a more extensive list of examples in any application guidance.

Question 5(a) and 5(b) – pro forma information

(a) We agree with the Board's preliminary view to retain pro forma information. As mentioned in paragraph 2.73, information about the financial performance of the acquired business from the beginning of the current period to the acquisition date will help investors in the next reporting period. Post-acquisition, investors will be able to

compare the company's financial performance, which will include the acquired business for a full year, with its financial performance in the current period. This information also helps investors to estimate the future contribution of the acquired business to the future financial performance of the combined entity.

(b) To reduce diversity in practice in the content and preparation of pro forma information we recommend that the Board provide guidance for the preparation of pro forma financial information We are also of the view that the requirement of paragraph B64(q) of IFRS 3 *Business Combinations* about the impracticability of disclosing the information, and the reasons why the disclosure is impracticable, should be maintained.

Question 14 – audit considerations

Audit matters will be an important aspect of these requirements and should be considered as these proposals are finalized. For example, it will be important for auditors to understand how to assess completeness of business combination disclosures – specifically, which acquisitions are being monitored by management (CODM) and whether management has captured all metrics used to monitor whether the objectives for an acquisition are being met. Audit standard setters are therefore key stakeholders in this project; we encourage the IASB to address any questions or concerns raised by audit standard setters to help ensure consistent application of the proposals in the exposure draft.

II. Goodwill and Impairment

Question 9(a) and (c) – remove annual quantitative impairment test

(a) We think the Board should maintain the requirement to perform an annual quantitative impairment test as the proposal could make the impairment tests less robust and may exacerbate the issue discussed in paragraph 3.58 that impairment losses are already not recognised on a timely basis. Such a reduction in the robustness of impairment testing would not justify any potential reduction in cost.

Goodwill can represent a significant percentage of total assets for many companies, and we have seen companies where goodwill and intangible assets with indefinite useful lives represent more than 50% of total assets. In our view, requiring only a review of impairment indicators by management is insufficient to consider whether the carrying amounts may be impaired.

Also, as mentioned in paragraph 4.10, a simplification in IAS 36 *Impairment of Assets* ("IAS 36"), which allows an entity to use the most recently calculated recoverable amount in the current period's impairment test for a cash-generating unit ("CGU") containing goodwill, is already provided when certain criteria are meet. We recommend the Board consider why this existing simplification is not providing significant relief from having to perform annual impairment tests and consider whether the existing criteria in IAS 36.99 should be expanded and clarified (for example, by providing parameters of what is a "substantial amount") to allow for more opportunities for an entity to simplify its impairment test.

(c) In our view, the proposal to remove the requirement to perform an annual quantitative impairment test will make the impairment test process less robust. Indicators of impairment could appear gradually, especially when there is a slow deterioration of the financial performance of a CGU or a group of CGUs.

Removal of the annual test would likely place increased attention on the evaluation of indicators of impairment and the cost and complexity of the quantitative assessment may simply shift to the qualitative assessment. IAS 36 also requires the disclosure of information of interest to investors, such as the discount rate reflecting the risk specific to the asset, and growth rates. These inputs, which can provide investors with insight into management's assumptions, will no longer be disclosed unless a quantitative impairment test is performed. If the Board decides to remove the quantitative impairment test, we recommend the Board provide more guidance and examples of indicators, such as x% decline in revenue would be an example of an internal indicator. The Board should also consider requiring disclosure of the assumptions and judgments applied when there are "close calls" on determining if an indicator of impairment exist. We also suggest that the Board assess whether there need to be separate indicators of impairment for CGUs versus individual assets; bifurcating the indicators for CGUs could result in greater focus and clarity in assessing assets for impairment.

Question 10 – estimating value in use

The CAC generally supports the Board's preliminary view that it should develop proposals to remove the restriction prohibiting companies from including some cash flows in estimating value in use ("VIU") – cash flows arising from a future uncommitted restructuring, or from improving or enhancing the asset's performance. However, we share the concern outlined in paragraph 4.40 of the Discussion Paper, namely that without additional guidance on when to include restructuring cash flows in the VIU calculation, there is a risk that management may use inputs that are overly optimistic.

We are not convinced that the existing requirement requirements in IAS 36 would be sufficient to mitigate this concern. We are also concerned with the suggestion in paragraph 4.42 of the Discussion Paper that such a risk of over-optimism can be more effectively addressed by auditors and regulators. In particular, we are frequently required to challenge overly optimistic assumptions during our regulatory reviews which occur after financial statements are filed and made available publicly. Correcting these assumptions 'after the fact' does not result in timely information to investors, and we are concerned with the rationale discussed in paragraph 4.42 as a basis for the Board's preliminary view. We recommend that the IASB more effectively address this issue by developing further guidance on when to include cash flows arising from restructuring or enhancing the asset's performance in the VIU calculation.

We support the IASB's proposal to remove the explicit requirement to use pre-tax input and pre-tax discount rates to calculate VIU. We think that this could potentially reduce the complexity of the goodwill impairment test. In addition, using post-tax discount rates and post-tax inputs would be more consistent with other IFRS standards.

Question 11 – simplify the impairment test
We generally agree with the Board's preliminary view that it should not further simplify the impairment test in the manner outlined in paragraph 4.55(c) and (d) of the Discussion Paper.

However, with respect to paragraph 4.55(b), we observe that the simplifications to the impairment test that are the subject of the Board's preliminary view would make the VIU calculation more consistent with how fair value (and hence fair value less costs of disposal ("FVLCD")) is determined, if both are calculated on a discounted cash-flow basis. If the Board believes that there are still fundamental differences in VIU and FVLCD, we think the Board should provide more guidance on the difference between entity-specific inputs used in VIU and market-participant inputs used in FVLCD, as contemplated in paragraph 4.55(a) of the Discussion Paper.

Question 12 – intangibles to be included in goodwill
We support the Board's preliminary view that it should not develop a proposal to allow some intangible assets to be included in goodwill, as the recognition of intangibles assets separately from goodwill provides relevant and useful information for investors.

Our view is not impacted by the determination of whether amortisation of goodwill is reintroduced, as the useful life of some intangible assets may not be the same as the useful life of unidentifiable intangible assets within goodwill.

Question 13 – consistency with U.S. GAAP
Our responses to the questions in the Discussion Paper do not depend on whether the outcome is consistent with U.S. GAAP as it exists today, or as it may be after the Financial Accounting Standards Board's ("FASB's") current work. However, we encourage the Board to proactively communicate and work closely with the FASB so that convergence with U.S. GAAP in this area can be maintained.

We also note that stakeholders in Canada may react negatively if the final IASB requirements lead to a different accounting treatment for goodwill under IFRS than U.S. GAAP, as this would result in reduced comparability to U.S. companies.

If you have any questions about this letter, please do not hesitate to contact us.

Yours truly,

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