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Ref: EFRAG's due process on the IASB's Exposure Draft Business Combinations – Disclosures, Goodwill and Impairment

Dear Dr Klinz,

The European Securities and Markets Authority (ESMA) thanks you for the opportunity to contribute to EFRAG's due process with regards to Exposure Draft ED/2024/1 *Business Combinations – Disclosures, Goodwill and Impairment*. We are pleased to provide you with the following comments with the aim of improving the consistent application and enforceability of IFRS.

ESMA welcomes the IASBs' proposals to provide better information about the acquisition of businesses which address the requests of many users of financial statements.

ESMA agrees with the proposal – supported by EFRAG – to require entities to disclose information about the entity's acquisition-date key objectives and related targets for a business combination and whether these objectives and targets are being met. ESMA agrees that the information should only be provided for a subset of business combinations, which is based on a closed list of qualitative and quantitative conditions and finds the proposed quantitative thresholds adequate. ESMA highlights the need for sufficient transparency with regard to the entity's definition of the performance measures used for business combinations.

ESMA considers that exemptions from disclosure of certain information, due to its commercial sensitivity may only be justified in rare and clearly delineated circumstances. Against this background, ESMA considers that the proposed exemption from disclosing certain information is not specific enough. ESMA invites the IASB to include, within the standard, additional guidance and examples of situations in which the application of the exemption would be appropriate.

ESMA agrees with the proposal to require entities to disclose information about the performance of the business combinations that is reviewed by the entity's key management personnel, for as long as the performance of the business combination is reviewed.

ESMA also supports the requirement to disclose quantitative information about expected synergies in the year of acquisition. However, ESMA considers that, given that some synergies may take longer than the year of acquisition to materialise, an entity should also disclose in the subsequent years whether expected synergies have been achieved or whether they are still expected to be achieved.

While ESMA agrees with the proposed changes to the impairment test to reduce shielding and management over-optimism, ESMA does not expect these proposals to be very effective and encourages the IASB to discuss further improvements. ESMA considers that the IASB should also explore whether failure to meet key objectives and related targets of a business combination should be linked to, and have an effect on, the impairment testing.

ESMA has very strong concerns about the proposal to remove the current constraint on cash flows used to calculate value in use as the removal would potentially increase the effect of management over-optimism on the impairment test. Should the IASB pursue this proposal, further guidance and examples would be indispensable. In this vein, ESMA, similarly to EFRAG, considers that entities should be required to disclose the extent to which the calculated value in use is influenced by expected uncommitted future restructuring and enhancements.

Finally, ESMA agrees with the proposal to remove the requirement to use pre-tax cash flows and pre-tax discount rates in calculating value in use.

Our detailed responses are included in the Appendix to this letter. In case you have any questions or comments please do not hesitate to contact me or Isabelle Grauer-Gaynor, Head of the Corporate Finance and Reporting Unit (Isabelle.Grauer-Gaynor@esma.europa.eu).

Yours sincerely,

[Verena Ross]

Appendix

1 Disclosures: Performance of a business combination

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?

1. ESMA shares the view that it is currently challenging to assess the performance of the acquired business against management's expectations. ESMA highlighted in the past that the currently required disclosures on the reasons for a business combination and related synergies are often missing or boilerplate.¹ Therefore, ESMA welcomes the IASBs' proposals to provide better information about the acquisition of businesses which appear to be reflective of the requests of many users of financial statements.
2. ESMA agrees with the proposal to require entities 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. ESMA considers that this information about the performance of a business combination would help users to assess how effectively the entity's management has used the entity's economic resources to acquire businesses.
3. ESMA also agrees that the above information on the performance of a business combination should be disclosed for a subset of an entity's business combinations, while entities continue to provide key qualitative information about all (material) business combinations (strategic rationale for the business combination and a qualitative description of the factors that make up the recognised goodwill). In ESMA's view it is important that such a subset is clearly defined, and that the definition is sufficiently robust to ensure that the disclosed information provides an appropriate basis for investors' decisions. For our comments on the definition of the subset proposed in the ED, we refer to our response to Question 2.
4. ESMA considers that commercial sensitivity is generally not a valid reason for not informing investors. Therefore, exemptions from disclosure of information that provides an important basis for investors' decisions can only be justified in very rare exceptional circumstances. For our detailed comments on the criteria for the application of the exemption proposed in the ED, we refer to our response to Question 3.
5. Finally, ESMA shares the view that the proposed disclosures should be made in the financial statements (and not as part of the management commentary) as this will ensure that this information is audited and enforceable. In this regard, ESMA agrees that auditors will be able to verify (i) whether the information disclosed is the information an entity's key management personnel receive to review a business combination and (ii) whether there is adequate explanation and appropriate evidence supporting the information.

¹ See ESMA Report Review on the application of accounting requirements for business combinations in IFRS financial statements ([ESMA/2014/643](#))

2 Disclosures: Strategic business combinations

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?

6. ESMA agrees with the use of a threshold approach to define the subset of business combinations for which additional information would be of particular importance to users of financial statements. The use of a closed list of conditions (thresholds) would improve the enforceability and comparability of information on business combinations. In ESMA's view, a more principle-based open-list approach would require here a very high level of judgement and would often result in practical challenges or incorrect application.
7. ESMA also agrees with the qualitative and quantitative thresholds proposed by the IASB and finds the threshold level set for the quantitative thresholds (10%) adequate. ESMA notes positively that these thresholds are already included in other IFRS standards (IFRS 5, IFRS 8) and they will therefore be familiar to entities applying IFRS. A higher threshold than 10% would most likely lead to the loss of important decision-relevant information. ESMA, therefore, strongly advises against any relaxation of these thresholds. In addition, ESMA considers that it would be useful if the IASB provided additional clarification on when an entity acquires a business which significantly increases - at entity level - a line of business in which the entity had only a small/minor level of activity prior to the business combination.

8. ESMA also supports the proposal that an entity discloses information about a business combination if the business combination meets at least one of the thresholds. ESMA does not share the concerns expressed by some preparers that providing information for all business combinations that meet the proposed thresholds would be too burdensome. ESMA notes that the proposed disclosures only include information that is readily available to entities as this information is reported to and reviewed by the entity's management.
9. The IASB uses the notion of 'strategic business combinations' for the subset of business combinations for which disclosures should be provided. ESMA notes that paragraph BC54 defines a strategic business combination as a business combination 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. ESMA considers that this definition might be too narrow to be an appropriate starting point for defining a relevant subset of business combinations, as users may need additional information for some business combinations which do not meet this condition. Therefore, we suggest that the IASB removes the description of a strategic business combination in BC54 and BC55.
10. ESMA notes that the key objectives and related targets used by entities to assess the performance of their business combination would often not meet the definition of management performance measures in IFRS 18. ESMA emphasises the need for sufficient transparency regarding the entity's definition of the performance measures used for business combinations. ESMA notes that paragraph BC38 of the Basis for Conclusions explains that targets need to be specific enough to verify whether the objectives are being met and includes some examples of targets. However, ESMA considers that more specific requirements should be included in the text of the standard as the guidance included in the Basis for Conclusions would not be sufficient to effectively enforce transparency.
11. Finally, ESMA notes that Figure 1 immediately following paragraph B67C, which according to paragraph B67C demonstrates the application of paragraphs B67A-B67C, appears to show only the application of paragraphs B67A and B67B.

3 Disclosures: Exemption from disclosing information

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 achieving that aim.**

12. ESMA considers that the condition for applying the exemption from disclosure of information in paragraph B67D of the ED ('disclosing information can be expected to prejudice seriously the achievement of any of the entity's acquisition-date key objectives for the business combination'), accompanied by a non-exhaustive list of (two) factors to be considered to determine whether an item of information is eligible for the exception in the same paragraph, is not specific enough to prevent entities from inappropriately omitting the disclosure. ESMA sees a risk that the rather vague wording ('can be expected') could incentivise entities to regularly apply the exception in situations where the information is not already publicly available.
13. ESMA also notes that the exemption proposed in the ED refers to a much broader and more diverse fact pattern than the exemption in paragraph 92 of IAS 37 *Provisions, Contingent Liabilities and Contingent Assets*, which is also aimed at preventing negative consequences for entities of disclosing some sensitive information. The disclosure exemption in IAS 37 is applied in situations where the entity is in dispute which implies its awareness of the exact nature of the threats to its interests and also existence of a clearly identifiable opponent – another party that could take advantage of the disclosures. Therefore, in practice there are few opportunities to misuse paragraph 92 of IAS 37.
14. In ESMA's view, additional guidance and examples of situations in which the application of the exemption would be appropriate should be provided in order to ensure that the exemption is only applied in very rare circumstances ESMA considers that such situations would primarily exist if the required disclosures would lead to the publication of information whose public disclosure is not permitted by law or would have severe adverse legal consequences. ESMA also proposes that when applying paragraph B67E of the ED entities should be required to make every reasonable effort to ensure that the overall relevance of the disclosure on the concerned business combination is not impaired.²
15. ESMA agrees that entities that apply the exception should (i) disclose this fact and the reasons for omitting disclosure of an item of information and (ii) reassess at the end of each

² We refer to a similar requirement in the European Sustainability Reporting Standards (ESRS) paragraph 108 of ESRS 1 *General Requirements*.

reporting period whether the item of information is still eligible for the exemption, as required in paragraphs B67E and B67G of the ED

4 Disclosures: Identifying information to be disclosed

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:
- 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?
 - 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?

16. ESMA agrees with the proposal to require entities to disclose information about the performance of the business combinations that is reviewed by the entity's key management personnel for as long as the entity's key management personnel reviews the performance of the business combination.
17. ESMA notes that, according to paragraph B67B of the ED, if the entity's management has stopped reviewing the performance of an acquisition-date key objective and the related targets after the end of the second annual reporting period after the year of acquisition, this fact and the reasons for doing so are not required to be disclosed. Given that management's objectives for many business combinations are long-term in nature and the business plans cover periods longer than two years³, providing this information for a longer period of time in line with the management's expectations of when the acquisition objectives/targets will be achieved appears to be more appropriate.

5 Disclosures: Other proposals

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 BC23–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)

³ See for example paragraph B18 IFRS S2 which refers to a multi-year strategic planning cycle (for example, every three to five years).

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?

18. ESMA supports amendments to the disclosure requirements in IFRS 3 referred to in Question 3. In particular, ESMA supports the requirement to disclose quantitative information about expected synergies in the year of acquisition. However, ESMA is of the opinion that an entity should also disclose in the subsequent years whether expected synergies have been achieved in the reporting period and whether they are still expected to be achieved in the future or alternatively explain why this information is not monitored by management.

19. ESMA acknowledges that disclosing information about achievement of the expected synergies in the subsequent years would be required under the ED’s current proposals on disclosing information about the performance of a business combination, if the entity’s key management personnel decide to assess whether expected synergies have been achieved in reviewing the performance of the business combination. However, ESMA notes that synergies regularly play a significant role in the rationale for business combinations and give rise to the recognition of goodwill. Therefore, ESMA considers that this additional information about synergies would be very helpful in assessing the success of an acquisition and might provide useful indications with regard to management stewardship and impairment of the recognised goodwill or intangible assets.

6 Changes to the impairment test

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?

20. ESMA recognises the IASB's continued efforts to respond to requests of many stakeholders and make the impairment test more effective. While ESMA agrees with the IASB's proposals to reduce shielding and management over-optimism, ESMA does not expect these proposals to be very effective and have significant impact on the performance of impairment tests as they do not significantly change the current requirements. Therefore, ESMA encourages the IASB to redeliberate further improvements, such as:

- Providing further guidance on ‘reasonable and supportable assumptions’,⁴
- Providing examples for the application of guidance in the new paragraphs 80A and 80B on the determination of the highest level at which an entity is permitted to allocate goodwill,
- Requiring entities to disclose the extent to which the forecast cash flows of prior years used in impairment tests diverged from actual cash flows of the relevant years.

21. ESMA also suggests that the IASB investigates whether requirements similar to those included in current paragraph 80 and proposed paragraphs 80A and 80B of IAS 36 could be introduced for corporate assets (i.e. CGUs to which corporate assets are allocated cannot be larger than an operating segment) as this may help to reduce shielding.
22. Moreover, ESMA notes that while paragraph 33(b) of IAS 36 currently requires entities to base cash flow projections used in measuring value in use on the most recent financial budgets/forecasts approved by managements, paragraph 38 of IAS 36 states that an entity considers whether financial budgets/forecasts represent management’s best estimate. ESMA considers that it should be clearly stated that information in management’s financial budgets/forecast should be adjusted for the purposes of the measurement of value in use, if this information does not reflect best estimates.
23. ESMA also refers to its proposals on overoptimistic cash flows and on the shielding effect included in ESMA’s comment letter on the IASB’s Discussion Paper Business Combinations - Disclosures, Goodwill and Impairment.⁵
24. Moreover, ESMA notes that a reallocation of goodwill between the cash generating units in the subsequent periods may be used to avoid the recognition of an impairment loss. Therefore, ESMA considers it useful to require entities to explain changes in the carrying amount of goodwill allocated to a cash-generating unit and how these changes may affect the recognition of a goodwill impairment. Moreover, ESMA sees merit in requiring an impairment test immediately before reallocating goodwill if there have been significant changes in the key assumptions since the last impairment test that could lead to an impairment of goodwill. If an impairment is identified, it shall be recognised before the goodwill is reallocated.
25. In addition, ESMA notes that the requirement to use a relative value approach in paragraph 87 of IAS 36⁶ may, in certain circumstances, result in an unjustified allocation of goodwill. This is particularly relevant when an acquired business is allocated to one CGU as a whole and a part of it performs significantly below management’s expectations with the consequence that this part is subsequently sold. For example, when the acquired company consists of two divisions and one of these divisions subsequently performs significantly worse and the other significantly better than management’s expectations, the relative

⁴ ESMA notes that some other IFRS that use the term ‘reasonable and supportable information’ provide some further guidance/examples (e.g. paragraph B50 of IFRS 17).

⁵ [esma32-61-413_esmas_cl_to_iasb_dp_goodwill_and_impairment.pdf\(europa.eu\)](#)

⁶ Unless the entity can demonstrate the superiority of some other method.

values of the divisions may change to a great extent from the time of the acquisition. As a result, only a small proportion of the acquired goodwill will be allocated to the underperforming division upon its disposal. ESMA encourages the IASB to consider whether the entity should be required to use an approach other than the relative value approach in the case of reorganisations (at least in certain circumstances).

26. ESMA would also find it very useful if the IASB explained (e.g. in the Basis for Conclusions) that, for the purpose of impairment testing goodwill acquired in a business combination cannot be allocated to a CGU that include assets (and liabilities) assigned to two or more reporting segments (even if these assets only account for a small proportion of all assets assigned to these segments) as this violates the requirement in paragraph 80(b) of IAS 36. In other words, the recoverable amount can only be calculated for a CGU whose assets belong to the same segment. ESMA considers that this explanation would contribute to correct application of the existing IAS 36 requirements.
27. Finally, ESMA considers that the IASB should explore whether failure to meet management's reported objectives and targets should be linked to and have an effect on the impairment test (e.g. entities should be required to assess and possibly disclose the effect of such failure on the cashflows applied for calculation of value in use; the failure should be viewed as an indication of impairment that may trigger performance of an impairment test before the regular annual impairment test). Such linkage would increase the usefulness of the disclosures significantly.

7 Changes to the impairment test: Value in use

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?

28. ESMA has very strong concerns about the proposal to remove a constraint on the inclusion in the value in use calculation of 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.⁷ ESMA considers that without additional safeguards the proposal will most likely increase the effect of management over-optimism on the impairment test and will further exacerbate the problem of 'too little, too late'.
29. Should the IASB pursue this proposal, in order to limit possible negative effects, additional guidance and examples would be indispensable. In particular, explanations would be required to clarify the boundaries of the 'current condition' and the 'current potential' of an asset. These explanations should clarify the borderline between (i) maintaining the level of economic benefits arising from the assets in its current condition and (ii) creating new economic benefits associated with a changed condition of the asset. Also, it should be explained when an asset has current potential to be restructured, improved or enhanced and how to determine whether certain cashflows are connected with this potential.
30. It would also be helpful to provide examples of situations when it would be appropriate to consider cashflows resulting from uncommitted restructurings when calculating value in use and when it would not be appropriate.
31. Moreover, ESMA considers that entities should be required to provide quantitative disclosures on the extent to which the calculated value in use is influenced by expected cash flows resulting from uncommitted future restructuring and enhancements. These disclosures would help users of the financial statements to better assess the impact of management's assumptions and estimates which may involve a particularly high degree of subjectivity and uncertainty (such as enhancement to the performance of assets that may never occur or investments which may be cancelled or postponed).
32. ESMA agrees with the proposal to remove the requirement to use pre-tax cash flows and pre-tax discount rates in calculating value in use. ESMA notes, however, that it would be useful to clarify what impact this change would have on the application of the guidance in paragraph 78 of IAS 36 on deferred tax liabilities.

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

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:

⁷ For more details, ESMA refers to its [comment letter](#) on the IASB's Discussion Paper *Business Combination – Disclosure, Goodwill and Impairment*.

- 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?

33. ESMA does not have any comments on this question.

9 Transition

Question 9 – Transition (proposed paragraph 64R of IFRS 3, proposed paragraph 140O 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.

34. ESMA does not have any comments on this question.