22 July 2014

Mr Hans Hoogervorst
Chairman
International Accounting Standards Board
30 Cannon Street
London EC4M 6XH
UNITED KINGDOM

Dear Hans

AOSSG comments on IASB Request for Information *Post-Implementation Review of IFRS 3 Business Combinations*

The Asian-Oceanian Standard-Setters Group (AOSSG) is pleased to provide comments on the IASB Request for Information (RFI) *Post-Implementation Review (PIR) of IFRS 3 Business Combinations.* In providing this feedback, the AOSSG sought inputs from its constituents within each jurisdiction.

The AOSSG currently has 26 member standard-setters from the Asia-Oceania region: Australia, Brunei, Cambodia, China, Dubai, Hong Kong, India, Indonesia, Iraq, Japan, Kazakhstan, Korea, Macao, Malaysia, Mongolia, Nepal, New Zealand, Pakistan, Philippines, Saudi Arabia, Singapore, Sri Lanka, Syria, Thailand, Uzbekistan, and Vietnam.

To the extent feasible, this submission to the IASB reflects in broad terms the collective experiences of AOSSG members. Each member standard-setter may also choose to make a separate submission that is consistent or otherwise with aspects of this submission. The intention of the AOSSG is to enhance the input to the IASB from the Asia-Oceania region and not to prevent the IASB from receiving the variety of inputs that individual member standard-setters may wish to submit. This submission has been circulated to all AOSSG members for their feedback after having initially been developed through the AOSSG Acquisitions and Reporting Entity Issues Working Group.

Overall, AOSSG members were informed that constituents generally thought that IFRS 3 promoted useful financial information, but many expressed concerns with regard to the following matters:

(a) Whether information resulting from the non-amortisation of goodwill and intangible assets with indefinite lives is useful, and whether the level of subjectivity and costs relating to annual impairment testing is sufficiently justifiable (see our comments on Question 5);

(b) Whether fair value information presented on the statement of financial position for separately recognised intangible assets is sufficiently useful even with its high degree of subjectivity (see our comments on Question 4); and

(c) Whether disclosures required of pro-forma financial information is useful (see our comments on Question 8).

Inputs from the AOSSG to specific questions in the RFI are explained in more detail in the Appendix. If you have any questions regarding any matters in this submission, please contact either one of us.

Yours sincerely,

Clement Chan
AOSSG Chair

Yukio Ono
AOSSG Acquisitions and Reporting Entity Issues Working Group Leader

APPENDIX – Detailed comments from the AOSSG on Specific Questions in the IASB RFI PIR of IFRS 3

Question 1- Background and Experience

Please tell us:

(a) about your role in relation to business combinations (ie preparer of financial statements, auditor, valuation specialist, user of financial statements and type of user, regulator, standard-setter, academic, accounting professional body etc).[(a)]

(b) your principal jurisdiction. If you are a user of financial statements, which geographical regions do you follow or invest in?

(c) whether your involvement with business combinations accounting has been mainly with IFRS 3 (2004) or IFRS 3 (2008).

(d) if you are a preparer of financial statements:

(i) whether your jurisdiction or company is a recent adopter of IFRS and, if so, the year of adoption; and

(ii) with how many business combinations accounted for under IFRS has your organisation been involved since 2004 and what were the industries of the acquirees in those combinations.

(e) if you are a user of financial statements, please briefly describe the main business combinations accounted for under IFRS that you have analysed since 2004 (for example, geographical regions in which those transactions took place, what were the industries of the acquirees in those business combinations etc).

(a) Type of user includes: buy-side analyst, sell-side analyst, credit rating analyst, creditor/lender, other (please specify).

Responses to Question 1

1 Please see the following for our response to the above questions.

(a) The AOSSG is a group of accounting national standard-setters from the Asia-Oceania region

(b) Member jurisdictions are Australia, Brunei, Cambodia, China, Dubai, Hong Kong, India, Indonesia, Iraq, Japan, Kazakhstan, Korea, Macao, Malaysia, Mongolia, Nepal, New Zealand, Pakistan, Philippines, Saudi Arabia, Singapore, Sri Lanka, Syria, Thailand, Uzbekistan, and Vietnam

(c) Some member jurisdictions have applied IFRS 3 (2004) and subsequently have been applying IFRS 3 (2008). Many member jurisdictions have just adopted IFRS in recent years, and accordingly, have been applying IFRS 3 (2008) since initial application.

(d) : N/A

(e) : N/A

Question 2: Definition of a Business

(a) Are there benefits of having separate accounting treatments for business combinations and asset acquisitions? If so, what are these benefits?

(b) What are the main practical implementation, auditing or enforcement challenges you face when assessing a transaction to determine whether it is a business? For the practical implementation challenges that you have indicated, what are the main considerations that you take into account in your assessment?

Responses to Question 2(a)

2 Most AOSSG member were informed that the separate accounting treatments for business combinations and asset acquisitions are generally appropriate because many consider that different economic substances are derived from the acquisition of a business versus the acquisition of an asset. The value of a purchased asset or group of assets in the context of a business combination typically includes value of both identifiable assets and non-identifiable assets including intangible assets, where the profitability of the asset group (including goodwill) is typically reflected in the value of the assets when acquired as a business combination. This is not the case with asset acquisitions. Accordingly, many of our constituents thought that the accounting treatments should be separate for business combinations and asset acquisitions.

3 Nevertheless, our members were informed that the different accounting outcomes arising from a business acquisition and an asset acquisition has influenced the way in which entities apply judgement on the assessment of whether an acquisition relates to a business or an asset.

Responses to Question 2(b)

4 Many AOSSG members were informed that the main practical challenge in assessing whether a transaction relates to a business is the lack of clarity as to what constitutes a 'business'. This may be attributed to the lack of guidance in Standards or the nature of the transaction itself, which can be complex. This has led to challenges in determining whether an acquisition relates to a business combination or an asset acquisition, and in determining which standard to apply.

5 For example, while IFRS 3 provide definitions and related explanations in paragraphs B7 to B9, it does not provide explicit guidance as to what constitutes 'inputs and processes' to meet the definition of a business. Consequently, different views have developed in practice whether a transaction relates to a business combination or asset acquisition. Our members were informed that this is an issue particularly in the mining, real estate, hospitality, shipping and pharmaceutical industries in many jurisdictions.

Question 3: Fair Value

(a) To what extent is the information derived from the fair value measurements relevant and the information disclosed about fair value measurements sufficient?[(a)] If there are deficiencies, what are they?

(b) What have been the most significant valuation challenges in measuring fair value within the context of business combination accounting? What have been the most significant challenges when auditing or enforcing those fair value measurements?

(c) Has fair value measurement been more challenging for particular elements: for example, specific assets, liabilities, consideration etc?

(a) According to the Conceptual Framework information is relevant if it has predictive value, confirmatory value or both.

Responses to Question 3(a)

6 AOSSG members found that our constituents generally consider the information derived from the fair value measurement to be relevant and sufficient.

7 However, our members received the following observations from constituents:

(a) Fair values of some intangible assets are highly subjective and less reliable, and such information may not be useful for users.

(b) Mixed views were expressed on the measurement requirements for equity instruments issued by an acquirer as consideration for a business combination. For such a transaction, IFRS 3 requires an entity to measure the consideration based on the fair value of those equity instruments at acquisition date, but the number of equity instruments to be issued by the acquirer is typically agreed upon based on the closing market prices of the instruments at the time of pre-acquisition negotiations. In many cases, the closing market prices at acquisition date would be higher than the closing market prices at the time of negotiations due to the market's positive reaction to the acquisition; and consequently, some constituents believe that goodwill amount is often inflated and therefore inappropriate. However, other constituents contend that measuring the equity instruments at fair value on acquisition date would faithfully represent, and provide relevant information about the value exchanged for the acquired business. They are of the view that the fact that the acquirer had assumed an exposure on its own equity instruments (rather than fixing the value of consideration and settling the required number of equity instruments based on the market price at acquisition date) ought to be reflected in the consideration and resultant goodwill.

(c) Although information about the valuation model and key assumptions in relation to the fair value measurement is only required for non-controlling interest and contingent consideration in IFRS 3, the same information should be required for assets and liabilities acquired under business combinations that are individually significant or of special nature, particularly when significant unobservable inputs (level 3) have been used in the valuation.

(d) Information regarding fair value measurement (including that required by paragraph 134 of IAS 36 *Impairment of Assets*) is often too voluminous. Many users have found it difficult to understand this type of information, including information on assumptions that management uses to estimate future cash flows.

Responses to Question 3(b)

8 AOSSG members were informed that there are various challenges in measuring fair value in the context of business combination accounting. This is largely due to the high degree of subjectivity and cost implications particularly when:

(a) measuring intangible assets;

(b) measuring cash-generating units (CGU); and

(c) determining control premium in step acquisitions.

9 Our members were informed that preparers and auditors found it particularly challenging to determine fair value of some assets and liabilities because of:

(a) a lack of active market for certain assets and liabilities;

(b) the nature of assumptions and inputs necessary to determine fair value, particularly for intangible assets. Further, our constituents have found that a broad range of fair values can be derived using different valuation models; and

(c) the availability of experts and acceptable valuation techniques and models.

10 Many members have found that preparers are facing significant cost implications, including the cost of experts and the entity's time and effort in obtaining relevant data, for determining fair value measurement of intangible assets. In addition, auditors are experiencing challenges in auditing the fair valuation of these assets.

Responses to Question 3(c)

11 AOSSG members found that fair value measurement of the following items particularly challenging for preparers and auditors:

(a) Contingent consideration and earn-outs;

(b) Intangible assets, such as intellectual property;

(c) Financial instruments that are unquoted; and

(d) Guarantees (as it requires the consideration of underlying risks, with respect to the probability and magnitude of risks, and discount rates).

Question 4: Separate Recognition of Intangible Assets from Goodwill and the Accounting for Negative Goodwill

(a) Do you find the separate recognition of intangible assets useful? If so, why? How does it contribute to your understanding and analysis of the acquired business? Do you think changes are needed and, if so, what are they and why?

(b) What are the main implementation, auditing or enforcement challenges in the separate recognition of intangible assets from goodwill? What do you think are the main causes of those challenges?

(c) How useful do you find the recognition of negative goodwill in profit or loss and the disclosures about the underlying reasons why the transaction resulted in a gain?

Responses to Question 4(a)

12 Many AOSSG members observed that users have found the recognition of separately identifiable intangible assets to be useful as it provides information about the current value of intangible assets and the reasons an acquirer is willing to pay a premium for the assets of the acquiree.

13 However, some members observed that preparers have found that identifying and recognising intangible assets as required by IFRS 3 to be very challenging and of limited use. These members also found that some preparers are of the impression that users in their jurisdictions do not really appreciate the difference between goodwill, brands and

other intangible assets, and accordingly, doubts the value in recognising separately identifiable intangible assets.

14 In addition, some members disagree with the presumption that an acquirer can always reliably measure intangible assets at fair value as long as they are separately identifiable. An example is an acquiree's internally generated brands and customer lists that cannot be distinguished from the business as a whole.

Responses to Question 4(b)

15 AOSSG members found that preparers have encountered the following challenges in separately recognising intangible assets:

(a) the identification of intangible assets (such as brands and customer lists);

(b) the measurability of intangible assets; and

(c) the cost benefit of separately recognising intangible assets.

16 Our members were informed that some preparers have found that separately recognising intangible assets to be counterintuitive when management does not intend on acquiring a particular intangible asset in a business combination. They believe that the exercise to separately identify intangible assets is solely for accounting purposes and has no significance and relevance to an entity's financial position.

17 In addition, our members were informed that some preparers believe that the measurement of intangible assets is not always reliable, and that the presumption in paragraph 35 of IAS 38 (that is, measurement of intangible assets can always be made reliably) does not hold true in practice.

18 Further, our members were informed that some preparers found that measurement of intangible assets give rise to significant cost implications, especially when valuation experts are involved.

Responses to Question 4(c)

(a) Usefulness of information resulted from recognition of negative goodwill in profit or loss and related disclosures

19 AOSSG members observed that users generally consider the recognition of negative goodwill in profit and loss and the disclosures about the underlying reason to be useful as they enhance transparency and the understanding of bargain purchase acquisitions.

20 However, some of our members were informed that some users and many think otherwise. For example, we received feedback that:

(a) there is no sound principle in immediately recognising negative goodwill in profit or loss, while goodwill is recognised as an asset. Symmetrical accounting is preferred and should be required.

(b) it would be more useful to separately disclose negative goodwill that relates to a bargain purchase from negative goodwill that is due to other expected negative events, such as, potential post-acquisition restructuring events. With that distinction, negative goodwill attributable to events other than a bargain purchase should be recognised in OCI at acquisition date until the expected event occurs (or over the period during which the effect of negative goodwill is expected to have an effect).

(c) Recognising gains or losses on negative goodwill is not rare in practice (i.e., bargain purchases happen not just in a forced sale but in the normal course of business), which is contrary to the presumption in IFRS 3.

Question 5: Non-amortisation of Goodwill and Indefinite-life Intangible Assets

(a) How useful have you found the information obtained from annually assessing goodwill and intangible assets with indefinite useful lives for impairment, and why?

(b) Do you think that improvements are needed regarding the information provided by the impairment test? If so, what are they?

(c) What are the main implementation, auditing or enforcement challenges in testing goodwill or intangible assets with indefinite useful lives for impairment, and why?

Responses to Question 5(a)

21 AOSSG members found that there are mixed views among users in relation to the usefulness of information resulting from annual impairment testing of goodwill and intangible assets with indefinite useful lives.

22 Our members found that many of our constituents (including users and preparers) question whether information from the current impairment-only approach is sufficiently useful, and instead forcefully suggested reintroducing a systematic amortisation of goodwill and intangible assets with indefinite useful lives while maintaining the requirement of impairment testing. For example, our constituents stated the following:

(a) Impairment charges often come late under the impairment-only approach, and investors usually factor in risks of impairment well before an impairment charge is recognised. One member found that the amount of amortisation expenses before adoption of IFRSs is much higher than that of impairment losses after adoption of IFRSs in its jurisdiction.

(b) Acquired goodwill is consumed and decreases over time, but the impairment-only approach does not reflect the effect, as it permits recognition of internally generated goodwill in place of the decrease in acquired goodwill.

(c) The recognition of impairment losses may be delayed due to the intermingling of future cash flows from acquired goodwill and unrecognised internally generated goodwill (both from existing business and newly generated over time as the business evolves). Management could also intentionally delay impairment recognition by allocating more goodwill to more profitable CGUs in the absence of guidance in IFRS 3 and managing key inputs within a range of acceptable values to achieve desired outcomes.

(d) In practice, the application of impairment testing is complicated, and subject to high degree of judgement. Thus, entities may not identify appropriate impairments on a timely basis.

(e) It is possible for entities to reasonably estimate a period over which acquired goodwill is consumed.

Responses to Question 5(b)

23 As mentioned in paragraph 21 above, AOSSG members found that some users are satisfied with the current impairment testing and consider no further improvement to impairment testing is needed, while many other users and preparers strongly consider requiring the amortisation of acquired goodwill and intangible assets would significantly promote the usefulness of financial information.

Responses to Question 5(c)

24 AOSSG members observed that preparers and auditors have faced the following implementation and auditing challenges in testing goodwill or intangible assets with indefinite useful lives:

(a) The choice of valuation models and making assumptions necessary for impairment testing, as it requires a significant degree of professional scepticism due to the fact that they are susceptible to management bias. It is challenging for auditors to verify these estimates and assumptions.

(b) The determination of recoverable amounts of cash-generating units to which goodwill or intangible assets with indefinite useful lives relate exacerbates the level of audit difficulty.

(c) The significant costs in annual impairment testing, especially due to, for example, reliance on valuation experts.

(d) The lack of expertise or skill to deal with measurement of intangible assets, especially in jurisdictions with emerging economies.

Question 6: Non-controlling Interests

(a) How useful is the information resulting from the presentation and measurement requirements for NCIs? Does the information resulting from those requirements reflect the claims on consolidated equity that are not attributable to the parent?

If not, what improvements do you think are needed?

(b) What are the main challenges in the accounting for NCIs, or auditing or enforcing such accounting? Please specify the measurement option under which those challenges arise.

To help us assess your answer better, we would be grateful if you could please specify the measurement option under which you account for NCIs that are present ownership interests and whether this measurement choice is made on an acquisition-by-acquisition basis.

Responses to Question 6(a)

25 AOSSG members observed that some of our constituents consider that the information resulting from the presentation and measurement requirements for NCI is generally useful.

26 Some of our members support retaining the fair value measurement as an option as they consider measuring NCI at fair value is consistent with

(a) the fair value measurement basis for assets and liabilities acquired; and

(b) the requirements of US GAAP.

27 These members suggested that consideration should be given to requiring one accounting policy choice to be applied to all business combinations, rather than for each combination.

28 However, our members were informed that many of our constituents consider providing an accounting option for an entity to measure NCI at fair value or as a proportionate share of the acquiree's net identifiable assets have caused a lack of comparability of financial statements across entities. Accordingly, these constituents consider that the accounting policy choice should be eliminated. In many jurisdictions, NCI is predominantly measured at the proportionate share in the recognised amounts of the acquiree's net identifiable assets, and accordingly, measurement on this basis is preferred.

Responses to Question 6(b)

29 AOSSG members observed various implementation challenges with regard to accounting for NCIs. For example, our constituents have found that it is not sufficiently clear whether a control premium should be excluded in measuring the fair value of equity instruments that are included as part of the consideration for a business. The inclusion of control premiums, or otherwise, has consequential effects on the fair value measurement of NCI in the acquiree. This issue is more prevalent to unlisted entities, but the estimation of a control premium lacks objectivity even when there are quoted market prices

Question 7: Step Acquisitions and Loss of Control

(a) How useful do you find the information resulting from the step acquisition guidance in IFRS 3? If any of the information is unhelpful, please explain why.

(b) How useful do you find the information resulting from the accounting for a parent's retained investment upon the loss of control in a former subsidiary? If any of the information is unhelpful, please explain why.

Responses to Question 7(a)

30 AOSSG members found that some of our constituents generally find the information on step acquisition to be useful.

31 However, our members were informed that many of our constituents are concerned about the usefulness of the following information:

(a) Acquired goodwill is often overstated due to gains recognised on previously held interests, especially when an acquiree's share price is inflated through a take-over bid.

(b) Purchasing additional shares is not always a significant event for the group, and there is no sufficient rationale for recognising gain/loss in profit or loss arising from the remeasurement when there is no movement in the previously held interests.

Responses to Question 7(b)

32 In line with our response in paragraph 30 of this letter, AOSSG members found that some of our constituents generally found the information on loss of control to be useful. However, our members were informed that many of our constituents have concerns similar to those stated in paragraph 31 above.

Question 8: Disclosures

(a) Is other information needed to properly understand the effect of the acquisition on a group? If so, what information is needed and why would it be useful?

(b) Is there information required to be disclosed that is not useful and that should not be required? Please explain why.

(c) What are the main challenges to preparing, auditing or enforcing the disclosures required by IFRS 3 or by the related amendments, and why?

Responses to Question 8(a)

33 AOSSG members were informed that our constituents are generally satisfied with the overall disclosure requirements in IFRS 3.

34 However, some members were informed that users would benefit from the following additional disclosures:

(a) A comparison between the projected future performance of an acquiree's business estimated at the time of acquisition and the actual performance in the subsequent periods; and

(b) Details of the acquisition-date fair value for each major class of consideration.

Responses to Question 8(b)

35 AOSSG members were not informed of specific information that should not be required.

Responses to Question 8(c)

36 Many AOSSG members were informed that preparers have found that providing pro-forma financial information relating to revenue and profit or loss of the combined entity for the current reporting period (as required by paragraph B64(q)(ii) of IFRS 3) to be too costly and of limited use. Furthermore, auditors have found significant challenges in verifying the information required in paragraph B64(q)(ii) especially when the business combination occurs close to the end of the reporting period.

37 In addition, our members were informed that some constituents expressed the following concerns:

(a) The disclosure requirements as a whole are excessive, which may have led entities in providing 'boiler-plate' disclosures.

(b) Some required information is commercially sensitive, especially where the business community is smaller and a specific entity can be identified easily.

Question 9: Other Matters

Are there other matters that you think the IASB should be aware of as it considers the PiR of IFRS 3?

The IASB is interested in:

(a) understanding how useful the information that is provided by the Standard and the related amendments is, and whether improvements are needed, and why;

(b) learning about practical implementation matters, whether from the perspective of applying, auditing or enforcing the Standard and the related amendments; and

(c) any learning points for its standard-setting process.

Responses to Question 9(a)

38 AOSSG members found that our constituents consider the following are common accounting issues that should be addressed:

(a) Business combinations under common control;

(b) Put options written on NCI; and

(c) Contingent consideration, including remeasurements, and the distinction between contingent consideration and employee compensation after acquisition date.

39 Having said that, some members do not think that major revisions to IFRS 3 are required, because many of the issues identified in practice relate to other IFRSs.

Responses to Question 9(b)

40 AOSSG members were informed that some constituents expressed concerns about the following matters:

(a) Paragraph B55 of IFRS 3 is confusing, and should be reworded to state that preparers should exercise judgment when determining whether a part of the contingent payment can be attributed to payment in exchange for an acquiree.

(b) It is sometimes unclear whether multiple transactions should be accounted for as a series of transactions that comprise a business combination or as separate transactions.

Responses to Question 9(c)

41 AOSSG members were informed that some constituents are concerned that IFRS 3 and the business combination standard in the US GAAP may diverge in the future.

Question 10: Effects

From your point of view, which areas of IFRS 3 and related amendments:

(a) represent benefits to users of financial statements, preparers, auditors and/or enforcers of financial information, and why;

(b) have resulted in considerable unexpected costs to users of financial statements, preparers, auditors and/or enforcers of financial information, and why; or

(c) have had an effect on how acquisitions are carried out (for example, an effect on contractual terms)?

Responses to Question 10(a)

42 AOSSG members were informed that IFRS 3 as a whole has improved the quality of financial information in relation to business combinations, including the following areas:

(a) Fair value measurement of acquired assets and liabilities;

(b) The quality of disclosures with regard to business combinations have improved; and

(c) Separate recognition of intangible assets in business combinations, which have assisted users in better understanding all assets acquired in the business combinations.

Responses to Question 10(b)

43 As mentioned earlier, AOSSG members were informed that the following areas have resulted in considerable unexpected costs to users, preparers, auditors and regulators:

(a) The requirements relating to separate recognition of intangible assets, including increased reliance on expert valuations (see paragraph 18 of this letter);

(b) The requirements relating to annual impairment testing of goodwill (see paragraph 24 of this letter); and

(c) The disclosure requirement for pro-forma financial information (see paragraph 36 of this letter).

Responses to Question 10(c)

44 AOSSG members have not received strong indication that IFRS 3 and related standards have had a significant effect on how acquisitions are carried out.

45 Nevertheless, our members received the following observations:

(a) Managements have had to re-examine their contractual clauses associated with acquisitions particularly in relation to the cash component of earn-outs.

(b) Given that contingent consideration may be required to be measured at fair value through profit or loss subsequently in accordance with paragraph 58 (b) of IFRS 3, entities may be incentivised to manipulate accounting profit after acquisition date by structuring the terms of the contingent consideration.

(c) The requirement to remeasure previously held interests at acquisition date fair value and to recognise the remeasurement difference in profit or loss may provide opportunity for structuring of business combinations.