The LIAJ’s Comments on the Discussion Paper

Business Combinations-Disclosures, Goodwill and Impairment

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The Life Insurance Association of Japan (LIAJ)

Contents

I. General comments on the Discussion Paper

1. We, The Life Insurance Association of Japan (or the "LIAJ"), would like to extend our gratitude to the International Accounting Standards Board (or the "IASB") for providing us with the opportunity to submit comments on the Discussion Paper, *Business Combinations - Disclosures, Goodwill and Impairment* (hereinafter referred to as the "DP"), published in March 2020.

2. The LIAJ is a trade association comprised of all 42 life insurance companies operating in Japan. Its goals are to promote the sound development of the life insurance industry in Japan, maintain its trustworthiness, and thereby contribute to improving the quality of life in Japan. The LIAJ would like to respectfully request the IASB to carefully consider the comments submitted from the sole representative body of the life insurance industry in Japan, which accounts for approximately 12%[1] of the world's life insurance premiums.

3. Insurers in Japan have the characteristics of being both users and preparers of financial statements. From the standpoint of users, the LIAJ believes it is integral for users to be provided with useful information, which contributes to their decision making. On the other hand, from the standpoint of preparers, the LIAJ believes it is not appropriate for preparers to incur significant costs in preparing financial statements. Therefore, the LIAJ recognizes that striking a balance between the needs of users and costs of preparers from a cost-benefit perspective should be always pursued.

4. As stated in the DP, the objective of the IASB's research project on goodwill and impairment is to explore whether companies can, at a reasonable cost, provide investors with more useful information about the acquisitions those companies make. The LIAJ understand this concept is consistent with the above-mentioned cost-benefit perspective; therefore, the LIAJ agrees with the overall objective of this project in this context.

5. However, the LIAJ is concerned about certain preliminary views, which are included in the DP that fails to strike the balance mentioned above and adds significant costs on preparers.

6. To be specific, the LIAJ is concerned about the preliminary view stated in Section 2 – Improving Disclosures About Acquisitions. For example, the preliminary view, "A company should be required to disclose information about the management's objectives for an acquisition", is stated in the DP. The LIAJ is concerned this may lead to the disclosure of commercially sensitive information, and as a result add significant costs on preparers.

7. Even if companies provide such information, the LIAJ believes such information should not be disclosed in the notes to the financial statements. Such information is considered not appropriate because the information may go beyond the role of the notes to provide complementary information to the financial statements and is forward-looking.

8. Please refer to the LIAJ's detailed comments presented below as answers to questions 2, 4, and 5.

9. The LIAJ expects the IASB to closely examine the comments as it relates to the cost benefit

[1] Swiss Re Institute, *sigma* No 4/2020.

perspective received from stakeholders on the DP. The LIAJ also appreciates the IASB's efforts toward further improved deliberation in a way fundamentally consistent with the objectives set forth by the IASB for the research project on goodwill and impairment.

II. Responses to the questions

Question 2

Paragraphs 2.4–2.44 discuss the Board's preliminary view that it should add new disclosure requirements about the subsequent performance of an acquisition.

(a) Do you think those disclosure requirements would resolve the issue identified in paragraph 2.4—investors' need for better information on the subsequent performance of an acquisition? Why or why not?

(b) Do you agree with the disclosure proposals set out in (i)–(vi) below? Why or why not?

(i) A company should be required to disclose information about the strategic rationale and management's (the chief operating decision maker's (CODM's)) objectives for an acquisition as at the acquisition date (see paragraphs 2.8–2.12). Paragraph 7 of IFRS 8 Operating Segments discusses the term 'chief operating decision maker'.

(ii) A company should be required to disclose information about whether it is meeting those objectives. That information should be based on how management (CODM) monitors and measures whether the acquisition is meeting its objectives (see paragraphs 2.13–2.40), rather than on metrics prescribed by the Board.

(iii) If management (CODM) does not monitor an acquisition, the company should be required to disclose that fact and explain why it does not do so. The Board should not require a company to disclose any metrics in such cases (see paragraphs 2.19–2.20).

(iv) A company should be required to disclose the information in (ii) for as long as its management (CODM) continues to monitor the acquisition to see whether it is meeting its objectives (see paragraphs 2.41–2.44).

(v) If management (CODM) stops monitoring whether those objectives are being met before the end of the second full year after the year of acquisition, the company should be required to disclose that fact and the reasons why it has done so (see paragraphs 2.41–2.44).

(vi) If management (CODM) changes the metrics it uses to monitor whether the objectives of the acquisition are being met, the company should be required to disclose the new metrics and the reasons for the change (see paragraph 2.21).

(c) Do you agree that the information provided should be based on the information and the acquisitions a company's CODM reviews (see paragraphs 2.33–2.40)? Why or why not? Are you concerned that companies may not provide material information about acquisitions to investors if their disclosures are based on what the CODM reviews? Are you concerned that the volume of disclosures would be onerous if companies' disclosures are not based on the acquisitions the CODM reviews?

(d) Could concerns about commercial sensitivity (see paragraphs 2.27–2.28) inhibit companies from disclosing information about management's (CODM's) objectives for an acquisition and about the metrics used to monitor whether those objectives are being met? Why or why not? Could commercial sensitivity be a valid reason for companies not to disclose some of that information when investors need it? Why or why not?

(e) Paragraphs 2.29–2.32 explain the Board's view that the information setting out management's (CODM's) objectives for the acquisition and the metrics used to monitor progress in meeting those objectives is not forward-looking information. Instead, the Board considers the information would reflect management's (CODM's) targets at the time of the acquisition. Are there any constraints in your jurisdiction that could affect a company's ability to disclose this information? What are those constraints and what effect could they have?

10. As stated in the above general comments on the DP, insurers in Japan have the characteristics of being both users and preparers of financial statements. Therefore, the LIAJ believe it is important for the IASB to consider the following two conditions in developing requirements for International Financial Reporting Standards (or "IFRS"): (a) to provide users of financial statements with useful information, and (b) not to add significant costs on preparers of financial statements (i.e. cost-benefit perspective).

11. Accordingly, some requirements stated in the IASB's preliminary view may provide useful information to users of financial statements, which meets the objective of the first condition. However, the disclosure of such information may add significant costs on preparers, which results in overly adverse effects for meeting the second condition.

12. To be specific, in the preliminary view, companies are required to disclose management's objective for the acquisition, the metrics that management will use to monitor whether the objectives of the acquisition are being met, and the extent to which management's objectives for an acquisition are being met (hereinafter referred to collectively as "information on management's objectives"). The LIAJ is strongly concerned about disclosing information on management's objectives as it may lead to the disclosure of commercially sensitive information, and result in the addition of significant costs on preparers.

13. In Paragraph 2.11 (b) of the DP, the example for disclosing management's objectives is as follows: "to achieve additional sale of the company's own Product W in new Territory Y using the acquired sales channels of Company B". Even a relatively simplified disclosure similar to this example could result in sensitive information revealing the company's strategy.

14. Furthermore, if companies are required to disclose information on management's objectives, companies may need to disclose information about quantitative targets and time frames. If such information is known to its competitors and used as a reference, it could have an adverse effect on the companies' business development. In this case, the expected return of the acquisition may be diminished, and result in the impairment of corporate valuations.

15. Additionally, even if information on management's objectives is disclosed by the company, the LIAJ believes the placement of such information should not be in the notes to the financial statements.

16. First, the LIAJ believes such information should not be disclosed in the notes to the financial statements because disclosing information on management's objectives may go beyond the role of the notes to provide complimentary information to the financial statements.

17. As stated in the paragraph 3.3 (c) of *Conceptual Framework for Financial Reporting*, and paragraph 7 of the IAS 1 *Presentation of Financial Statements*, information to be disclosed in the notes to the financial statements includes disaggregation of the items presented in the financial statements, information of the recognised and non-recognised items including information about their nature and risk factors, and information about estimates (methods, assumptions and judgements used). The LIAJ believes the information on management's objectives is not relevant to be disclosed in the notes to the financial statements.

18. Second, the LIAJ believes such information should not be disclosed in the notes to the financial statements because the information on management's objectives relates to what events management presumes will occur in future reporting periods, thereby viewed as forward-looking information. It is the understanding of the LIAJ that financial statements together with their notes typically provide information associated with past events. Therefore the disclosure of forward-looking information in the notes to the financial statements is inappropriate.

19. With regard to forward-looking information, paragraph 3.6 of *Conceptual Framework for Financial Reporting* states information about possible future transactions and other possible future events (forward-looking information) is included in the financial statements if it satisfies both of the following conditions: (a) relates to the entity's assets or liabilities—including unrecognised assets or liabilities—or equity that existed at the end of the reporting period, or during the reporting period, or to income or expenses for the reporting period; and (b) is useful to users of financial statements.

20. However, the LIAJ is concerned that information on management's objectives, especially the metrics that management uses to monitor whether or not the objectives of the acquisition are being met, and the extent to which management's objectives for an acquisition are being met, would not satisfy the second requirement (i.e. it is not useful to users of the financial statements). For example, it is assumed the approaches management uses to monitor the subsequent performance of an acquisition (frequency, metrics, etc.) will vary from company to company. Therefore, the comparability of information between the companies could not be ensured and it would be difficult to deem the provided information as "useful to users of the financial statements".

21. Also, paragraph 3.6 of *Conceptual Framework for Financial Reporting* mentioned above states "Financial statements do not typically provide other types of forward-looking information, for example, explanatory material about management's expectations and strategies for the reporting entity". Given this description, the LIAJ understands that the IASB itself has a view that information about management's expectations and strategies per se is not disclosed in the notes and considers such information to be provided outside of the financial statements.

22. Furthermore, IFRS Practice Statement 1, *Management Commentary* includes forward-looking information and descriptions about the way companies explain management's objective and

strategies for achieving those objectives. It is also the understanding of the LIAJ that it is the view of the IASB that information about management's expectations and strategies per se should not be disclosed in the notes and such information should be provided outside of the financial statements.

23. The LIAJ believes the matters commented above in paragraphs 19 through 22 are not consistent with the IASB's preliminary view that information on management's objectives should be disclosed in the notes to the financial statements. Nonetheless, the DP does not sufficiently explain the reasons to why such information is required to be disclosed in the notes. The LIAJ would like to urge the IASB for a better explanation on this matter if the IASB would like to continue to take the preliminary view that information should be disclosed in the notes.

24. Lastly on adding supplementary explanations. In practice, the LIAJ believes allowing companies to communicate information on management's objectives outside of the financial statement would allow for originality and creativity in preparing their financial statements and provide users with useful information. The requirement for companies to disclose such information in the notes to the financial statements will instead likely reduce the companies' flexibility. As the IASB does not compare the pros and cons of disclosing information on management's objectives in the notes, the LIAJ would like the IASB to conduct further deliberation on this matter.

25. Based on the above-mentioned comments, the LIAJ's responses to each of the questions are presented below.

<Answer to Question 2 (a)>

26. Although the disclosure requirements stated in the preliminary view relate to the description stated in the paragraph 2.4 of the DP, the LIAJ does not feel those requirements resolve issues as intended by the IASB given that the requirements to disclose such information in the notes are instead likely to reduce the companies' flexibility.

<Answer to Question 2 (b) and (c)>

27. The LIAJ does not agree. Regarding 2 (b)(i), the LIAJ does not believe that disclosing information about the strategic rationale of an acquisition will immediately lead to the disclosure of commercially sensitive information. Nevertheless, the LIAJ believes companies should not be required to disclose such information in the notes.

<Answer to Question 2 (d)>

28. Concerns about commercial sensitivity could inhibit companies from disclosing such information. The LIAJ has strong concerns that disclosure requirements stated in the preliminary view may lead to the disclosure of commercially sensitive information.

<Answer to Question 2 (e)>

29. The LIAJ is not aware of any direct constraints in Japan that could affect a company's ability to

disclose such information. However, the LIAJ feels information on management’s objectives is forward-looking information and would not satisfy the two conditions stated in the paragraph 3.6 of *Conceptual Framework for Financial Reporting*. Therefore, the LIAJ believes that such information will not be considered as appropriate to be disclosed in the notes to the financial statements.

Question 4
Paragraphs 2.62–2.68 and paragraphs 2.69–2.71 explain the Board's preliminary view that it should develop proposals: ● to require a company to disclose: ○ a description of the synergies expected from combining the operations of the acquired business with the company's business; ○ when the synergies are expected to be realised; ○ the estimated amount or range of amounts of the synergies; and ○ the expected cost or range of costs to achieve those synergies; and ● to specify that liabilities arising from financing activities and defined benefit pension liabilities are major classes of liabilities. Do you agree with the Board's preliminary view? Why or why not?

30. The LIAJ has the same view on the disclosure requirements on when the synergies are expected to be realised, the estimated amount or range of amounts of the synergies, and the expected cost or range of costs to achieve those synergies (hereinafter referred to collectively as "information about synergies") similarly to the disclosure requirements for information on management's objectives. Such information would be considered inappropriate to be disclosed in the notes to the financial statements given that the information may lead to the disclosure of commercially sensitive information. Additionally, such information goes beyond the role of the notes to provide complementary information to the financial statements and is forward-looking.

31. Particularly with regard to information about synergies, such information may include relatively more assumptions than information on management's objectives. This may lead to highly uncertain information. Besides, the LIAJ has the view that it is extremely difficult to quantify information about synergies even if companies attempts to quantify such information. Additionally, the information could provide little or no comparability. The LIAJ is concerned that providing such information may result in confusing users of the financial statements.

32. Based on the above-mentioned comments, the LIAJ disagrees with the IASB's preliminary view on information about synergies. The LIAJ does not believe that describing the synergies expected from combining the operations of the acquired business with the company's business will immediately lead to the disclosure of commercially sensitive information. Nevertheless, the LIAJ believes companies should not be required to disclose such information in the notes.

Question 5
IFRS 3 Business Combinations requires companies to provide, in the year of acquisition, pro forma information that shows the revenue and profit or loss of the combined business for the current reporting period as though the acquisition date had been at the beginning of the annual reporting period. Paragraphs 2.82–2.87 explain the Board's preliminary view that it should retain the requirement for companies to prepare this pro forma information. (a) Do you agree with the Board's preliminary view? Why or why not? (b) Should the Board develop guidance for companies on how to prepare the pro forma information? Why or why not? If not, should the Board require companies to disclose how they prepared the pro forma information? Why or why not? IFRS 3 also requires companies to disclose the revenue and profit or loss of the acquired business after the acquisition date, for each acquisition that occurred during the reporting period. Paragraphs 2.78–2.81 explain the Board's preliminary view that it should develop proposals: ● to replace the term 'profit or loss' with the term 'operating profit before acquisition-related transaction and integration costs' for both the pro forma information and information about the acquired business after the acquisition date. Operating profit or loss would be defined as in the Exposure Draft General Presentation and Disclosures. ● to add a requirement that companies should disclose the cash flows from operating activities of the acquired business after the acquisition date, and of the combined business on a pro forma basis for the current reporting period. (c) Do you agree with the Board's preliminary view? Why or why not?

<Answer to Question (c)>

33. The LIAJ disagrees with the requirements that companies should disclose the cash flows from operating activities of the acquired business after the acquisition date, and of the combined business on a pro forma basis for the current reporting period.

34. Acquired businesses are usually integrated with existing business. In these cases, it would be extremely difficult for companies to identify cash flows only from the acquired business. Therefore, the LIAJ is concerned that this may add significant costs on preparers.