

September 2017

Agenda ref 23

April 2016

STAFF PAPER

IASB meeting

Project	Business Combinations under Common Control		
Paper topic	Cover paper		
CONTACT(S)	Anna Krasnodemska	akrasnodemska@ifrs.org	+44 (0)20 7246 6495
	Yulia Feygina	yfeygina@ifrs.org	+44 (0)20 7332 2743

This paper has been prepared for discussion at a public meeting of the International Accounting Standards Board® (“the Board”) and does not represent the views of the Board or any individual member of the Board. Comments on the application of IFRS® Standards do not purport to set out acceptable or unacceptable application of IFRS Standards. Technical decisions are made in public and reported in IASB *Update*.

Purpose of this paper

1. This paper introduces a series of papers on Business Combinations under Common Control (‘BCUCC’). It discusses:
 - (a) project background (paragraphs 4-10),
 - (b) overview of the research and outreach activities since the last discussion of the project by the International Accounting Standards Board (‘the Board’) (paragraphs 11-19),
 - (c) feedback received on BCUCC in the 2015 Agenda Consultation (paragraphs 20-30), and
 - (d) next steps (paragraphs 31-32).
2. Other papers in the series are:
 - (a) Agenda Paper 23A *Method(s) of accounting for BCUCC*—discusses the results of research and outreach on the method(s) that:
 - (i) *are* applied in practice to account for BCUCC, and

- (ii) interested parties think *should be* applied to provide useful information about BCUCC.
 - (b) Agenda Paper 23B *Application of the predecessor method*—discusses the results of research and outreach on how the predecessor method:
 - (i) *is* applied in practice, and
 - (ii) interested parties think *should be* applied to provide useful information about BCUCC.
3. All papers are for information only and there are no questions for the Board.

Project background

The issue

4. Business combinations under common control, including those undertaken in preparation for initial public offerings (IPO), are excluded from the scope of IFRS 3 *Business Combinations*. In the absence of specific accounting requirements for BCUCC, entities are required to develop and apply an accounting policy that results in relevant information that faithfully represents the transaction. In doing that, entities use the hierarchy in IAS 8 *Accounting Policies, Changes in Accounting Estimates and Errors* and consider the requirements of IFRS Standards dealing with similar and related issues or the recent pronouncements of other standard-setting bodies and other accounting literature. As a result, in practice entities account for BCUCC using the acquisition method as set out in IFRS 3 (by analogy) or using the so-called predecessor method (by reference to national GAAPs).
5. The acquisition method requires recognition of acquired net identifiable assets at their acquisition-date fair values and recognition of any goodwill or a gain from a bargain purchase that arises in the business combination. In contrast, in accordance with the predecessor method, net assets transferred in a BCUCC are recognised at their predecessor carrying amounts. In addition, because of different requirements in national GAAPs, there are differences in how the predecessor method is applied in practice.

6. Various interested parties, notably securities regulators, have raised concerns about the diversity in practice in accounting for BCUCC and have asked the Board to provide guidance in this area. This has been a particular concern for emerging economies. Some interested parties from emerging economies stated that BCUCC are very common in their jurisdictions.

Project objective

7. The research project is now at the development stage.
8. The project objective is to identify which method, or methods, would provide most useful information about BCUCC and in particular:
- (a) whether and when using the predecessor carrying amounts would be most appropriate, and
 - (b) whether and when using fair values would be most appropriate.

Tentative Board decisions to date

9. In June 2014, the Board discussed the scope of the project and tentatively decided that the project should consider:
- (a) business combinations under common control that are currently excluded from the scope of IFRS 3,
 - (b) group restructurings, and
 - (c) the need to clarify the description of business combinations under common control, including the meaning of ‘common control’.
10. The Board also tentatively decided to give priority to considering transactions that could affect third parties, for example, transactions undertaken in preparation for an IPO, which is an area of particular concern for securities regulators.

Overview of the research and outreach activities

11. Since the scope of the project was tentatively agreed by the Board, the staff have performed a range of research and outreach activities with different types of

interested parties from various jurisdictions, including users of financial statements, regulators, standard-setters, preparers and accounting firms in order to understand:

- (a) how BCUCC tend to be accounted for today;
- (b) information needs of users of financial statements in a BCUCC and in particular whether and how those information needs differ from users' information needs in a business combination that is not under common control; and
- (c) views of other interested parties on how BCUCC should be accounted for in order to provide useful information, and why.

12. The activities performed by the staff included:

- (a) request for information to national standard-setting bodies;
- (b) other outreach activities with various interested parties; and
- (c) a review of recent relevant publications, requirements in a sample of national GAAPs and a sample of guidance published by accounting firms.

13. In performing outreach activities, the staff sought to obtain a balanced representation from various types of interested parties with a particular focus on users of financial statements, and a balanced geographical representation.

Request for information to national standard-setters

14. In July 2014, the staff asked regional and national standard-setters to provide information about the reporting requirements in their jurisdictions for an entity that is undertaking an IPO, in particular in the scenario in which there is a group restructuring in preparation for an IPO. The purpose of the request was to understand the existing requirements and to assess the extent of diversity in practice.

15. The staff received 15 responses to this request, mostly from Asia-Oceania and Europe. A few responses were received from Middle East, North America and Africa.

Other outreach

16. Since the last discussion by the Board, the staff have discussed BCUCC at more than 30 meetings and calls with interested parties, including:
- (a) 14 meetings and calls with individual users of financial statements and user representative groups, including ones from Europe, Australia, Japan, Africa, South America, and Canada and a meeting with the Capital Markets Advisory Committee. In the discussions with users of financial statements, the staff asked for views on whether predecessor carrying amounts or fair values would provide the most useful information about BCUCC, and why.
 - (b) 3 meetings and calls with securities regulator representative groups, namely the European Enforcers Coordination Session, the European Securities and Markets Authority and the International Organization of Securities Commissions Committee 1. In the discussions with regulators, the staff both sought information about the current practice in accounting for BCUCC and views on how BCUCC should be accounted for, and why.
 - (c) 4 meetings and calls with national and regional standard-setters, namely 2 meetings with the Accounting Standards Advisory Forum (ASAF), a call with the Emerging Economies Group and a workshop with Asia-Oceania standard-setters. In the discussions with standard-setters, the staff sought both information about the current practice in accounting for BCUCC and views on how BCUCC should be accounted for, and why.
 - (d) A meeting with the Global Preparers Forum. At that meeting, the staff asked for views on whether the acquisition method or the predecessor method should be applied to account for BCUCC, and why.
 - (e) Meetings with representatives of accounting firms, standard-setters, and preparers in which the staff provided an update on the project and discussed approaches to accounting for BCUCC.

17. The project has also been discussed at 3 IFRS Conferences, at which participants provided input on issues they encounter in practice and their views on accounting for BCUCC.

Research

18. Since the last discussion by the Board, the staff have reviewed relevant accounting literature and recent publications, including:
- (a) Exposure Draft 60 *Public Sector Combinations*, published by International Public Sector Accounting Standards Board in January 2016;
 - (b) research papers presented at the June 2015 and December 2015 ASAF meetings by the Canadian Accounting Standards Board (AcSB) and the Hong Kong Institute of Certified Public Accountants (HKICPA);
 - (c) Research report No. 33 *Critical Perspectives in Accounting for Business Combinations Under Common Control* published by the Korea Accounting Standards Board in April 2013;
 - (d) a research paper published in 2012 by Korea Accounting Standards Board *Transactions under Common Control*;
 - (e) Discussion Paper *Accounting for Business Combinations Under Common Control* published by the European Financial Reporting Advisory Group and the Italian accounting standard-setter Organismo Italiano di Contabilità in 2011, and the subsequent Feedback Statement;
 - (f) a sample of guidance on accounting for BCUCC published by accounting firms;
 - (g) requirements for BCUCC set out in a sample of national GAAPs; and
 - (h) a sample of academic papers on BCUCC suggested by respondents to the 2015 Agenda Consultation.
19. In reviewing those publications, the staff sought to understand the existing and proposed guidance and practice in accounting for BCUCC, and the rationale for the approaches being applied or being proposed.

Feedback from the 2015 Agenda Consultation

Comment letters

20. Roughly half of the respondents to the 2015 Agenda Consultation¹, including a user representative group, ranked BCUCC as a project of high or medium importance and/or urgency. Only a few respondents stated that the project is of low importance and/or of low urgency.
21. All securities regulators and most standard-setters, accounting firms and accounting bodies who commented on the 2015 Agenda Consultation thought that the project was important and/or urgent.
22. In terms of geographical trends, much support for the project comes from emerging economies. All the respondents from Africa and most respondents from Latin America and Asia thought that the project was important and urgent. In addition, most respondents from Australia and New Zealand, as well as many international respondents, also thought that the project was important and urgent.
23. Respondents who ranked the project as important and/or urgent provided the following reasons for their views:
 - (a) high frequency of transactions;
 - (b) absence of guidance in IFRS Standards; and
 - (c) diversity in practice.
24. A few respondents commented on the scope of the project. Most of them asked the Board to broaden the scope of the project to include related party or common control transactions more generally.
25. Roughly half of the respondents did not provide a ranking for the project. These respondents were mainly users and preparers from Europe and North America.

¹ 119 comment letters have been received on the 2015 Agenda Consultation

Investor survey

26. To provide input for the development of the Board’s future agenda, the staff also conducted an online survey to understand the views of the investor community about the areas of financial reporting that are in the most urgent need of improvement.
27. Roughly half of the users of financial statements who participated in the survey² ranked BCUCC as a project of high or medium importance. That was consistent with the feedback from other types of interested parties who responded to the survey—roughly half of other respondents to the survey also ranked the project as of high or medium importance.
28. A few users of financial statements made specific comments regarding the need to address the diversity in accounting for BCUCC resulting from the gap in IFRS Standards. One of them also asked the Board to eliminate structuring opportunities that arise from lack of requirements in this area.
29. Some users of financial statements did not provide a ranking for the project and some, although a minority, ranked the project as of low importance.

Outreach

30. The staff also sought feedback on the 2015 Agenda Consultation and what the Board’s agenda priorities should be at meetings with various interested parties from various jurisdictions. BCUCC has been identified as an important topic at the November 2014 Advisory Council meeting, two meetings with European interested parties conducted jointly with EFRAG and at the February 2016 working breakfast with the Advisory Council members from emerging economies.

Next steps

31. In the coming months, the staff plan to present to the Board a series of papers that will:

² 86 users of financial statements participated in the Investor survey

- (a) discuss advantages and disadvantages of applying the acquisition method set out in IFRS 3 and predecessor method to account for BCUCC;
 - (b) discuss application of the predecessor method;
 - (c) provide staff recommendations on which method, or methods would be most appropriate for accounting for BCUCC, and why;
 - (d) consider remaining scope questions; and
 - (e) discuss what the next due process step in the research project should be.
32. The findings and the feedback in the research project will help the Board to decide whether to start a Standards-level project on BCUCC in the future.