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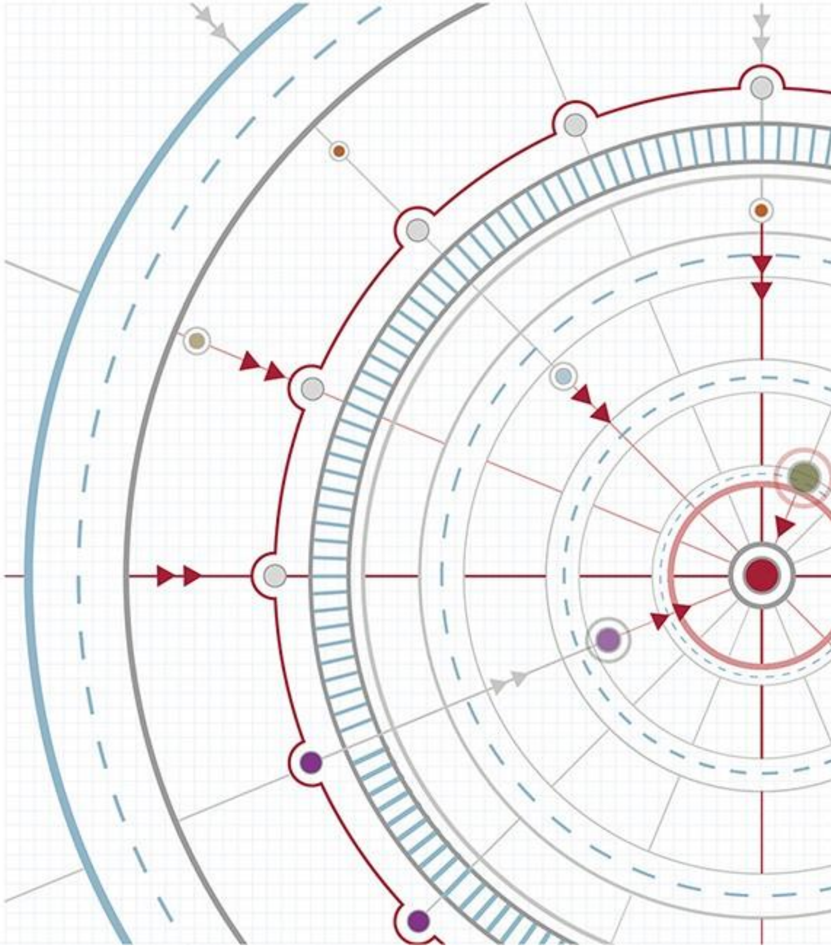

Business Combinations under Common Control

Slide deck ❷

Scope of the project

Emerging Economies Group Meeting
Sao Paulo, Brazil, December 2017

Meeting agenda

Background

Research and outreach

Next steps

Slide deck ❶

Scope of the project

Slide deck ❷

Methods of accounting

Slide deck ❸

Disclaimer

This paper has been prepared for discussion at a public meeting of the Emerging Economies Group (EEG). The views expressed in this paper do not represent the views of the International Accounting Standards Board (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*.

Project	**Business Combinations under Common Control (BCUCC)**		
Paper topic	Scope of the project		
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Overview of Slide deck ❷

Content

- 2014 tentative decision on the scope (slides 6-9)
- Clarifying the scope of the project:
  - Group restructurings (slides 13-22)
  - Business combinations vs BCUCC (slides 24-30)
- Illustrations of transactions within the scope (slides 32-37)
- Discussion (slide 39)

Objective

The objective of the session is to seek your views on the scope of the project

2014 tentative decision on the scope

2014 tentative decision on the scope

- **The Board tentatively decided that the project should consider:**
  - **business combinations under common control that are currently excluded from the scope of IFRS 3;**
  - **group restructurings; and**
  - **the need to clarify the description of business combinations under common control, including the meaning of 'common control'.**
- The Board also tentatively decided to **give priority to considering transactions that involve third parties**, for example those undertaken in preparation for an IPO. However, the Board did not restrict the scope of the project to such transactions only.
- The Board did not discuss which **reporting entity** and which **financial statements** of that reporting entity the project will focus on.

Considerations in setting the scope

- In setting the scope of the project, the Board considered:

Interaction with other Standards

	Transactions NOT under common control	Transactions under common control
NOT involving transfer of a **business**	Covered by applicable IFRS Standards	Covered by applicable IFRS Standards (scope exclusion do not apply)
involving transfer of a **business**	Covered by IFRS 3	Not covered by IFRS Standards

The staff will consider interaction with accounting for other transactions under common control as the project progresses (eg acquisition of associates, *see next slide*)

The staff will consider interaction with accounting for business combinations NOT under common control as the project progresses

Related IC topics—scope exclusions

IC submissions—2017

In **2017** the IFRS Interpretation Committee (IC) discussed:

- **can IFRS 3 scope exclusion for BCUCC be applied by analogy to other transactions under common control?**
  - IC tentative Agenda Decision—unless a Standard excludes transactions under common control from its scope, an entity applies the requirements in the Standard to those transactions.
- **how to account for an acquisition of an associate or of an interest in a joint venture under common control?**
  - the IC considered whether to apply the requirements in IAS 28 or the IFRS 3 scope exclusion for BCUCC;
  - the IC did not finalise its tentative Agenda Decision;
  - the staff will consider interaction between BCUCC and requirements in IAS 28 as the project progresses.

Clarifying the scope of the project

Clarifying the scope of the project

Group restructurings
(slides 12-21)

Not a defined term, and its meaning not described in IFRS Standards

Discussed at the October 2017 IASB meeting

BCUCC
(slides 23-29)

Described in IFRS 3, but there are **application questions**

Planned for discussion at the December 2017 IASB meeting

Clarifying the scope of the project

Group restructurings

Group restructurings

- The 2014 Board's tentative decision referred to group restructurings.
- However, **'group restructuring' is not a defined term** and is used differently by different parties.

Staff analysis (1/4)

‘restructuring’

… organising components of the whole in a different way

in a group

… organising **entities or business** within the group in a different way

Such changes in the group structure would involve **transferring entities or businesses between existing or newly created entities under common control**. Some such transfers would satisfy the description of BCUCC whereas others would not.

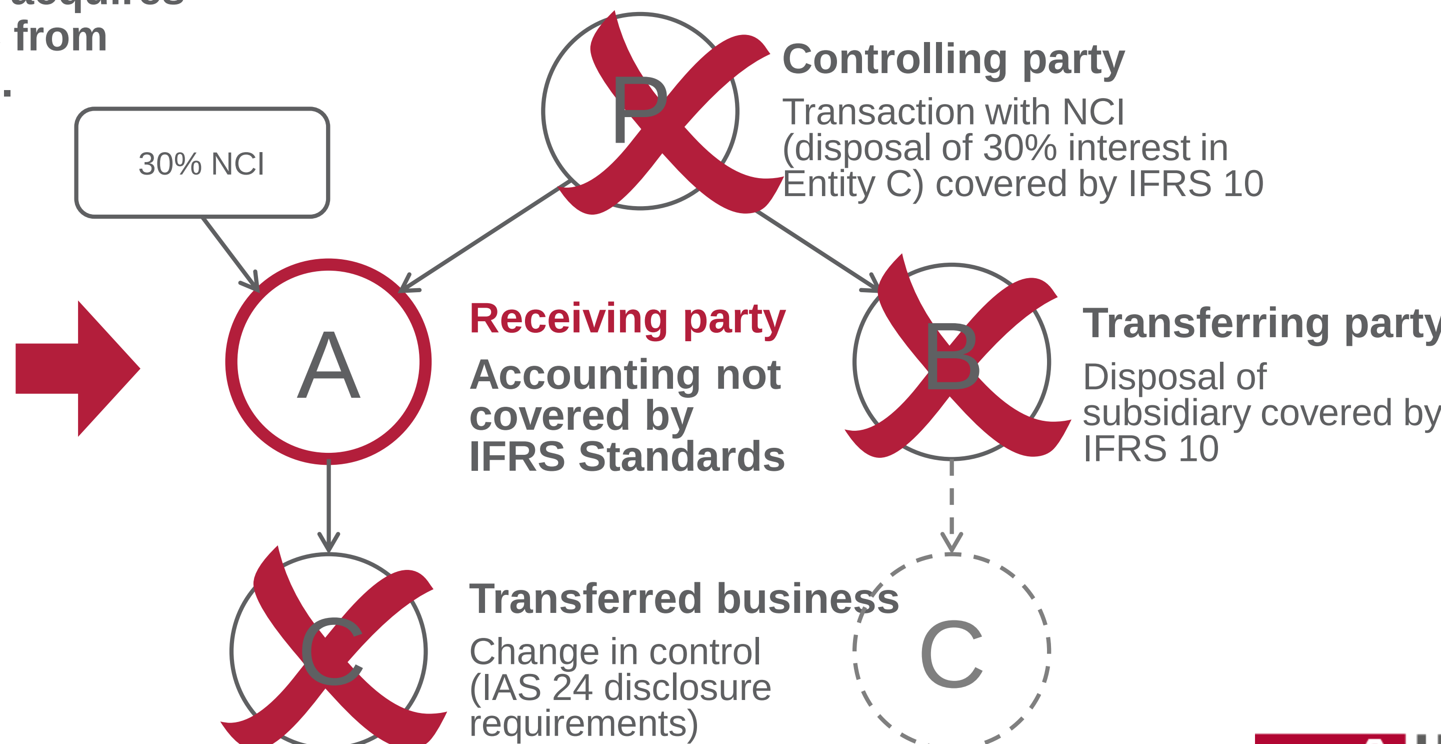
Staff analysis (2/4)

- To identify and describe the population of transactions that should be included in the scope of the project, the staff analysed a broad group of transactions that involve restructuring the relationships between entities or businesses under common control.
- The staff noted that regardless of whether a transfer of an entity or business within a group satisfies the description of a business combination under common control, any such transfer would involve the following parties:
  - **the controlling party or parent;**
  - **the transferring party;**
  - **the transferred party (entity or business); and**
  - **the receiving party.**

Staff analysis (3/4)

- Accordingly, a transfer of an entity or a business within a group can be analysed from the point of view of the parties involved in the transaction:

Entity A acquires Entity C from Entity B.



Staff analysis (4/4)

- A transfer of an entity or a business under common control may or may not satisfy the description of a BCUCC:
  - **if one of the combining parties can be identified as the acquirer** if IFRS 3 were applied, the transaction satisfies the description of a BCUCC and is included in the scope of the project in accordance with the Board’s 2014 tentative decision;
  - **if none of the combining parties can be identified as the acquirer** if IFRS 3 were applied, the transaction is not a BCUCC. However, accounting for such transactions is not addressed in IFRS Standards.

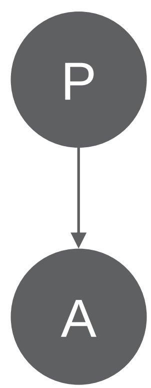
Related IC topics—one business (1/2)

IC submission—2011

- In **2011** the IC discussed a transaction where a Newco is established to acquire **one** other entity or business under common control.

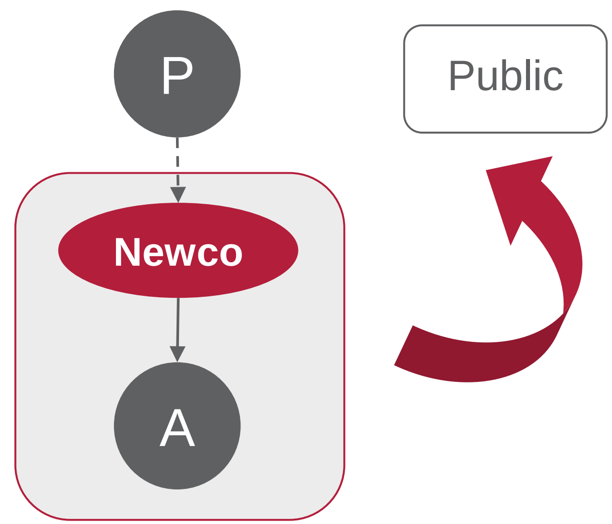
Before

Entity A is controlled and fully owned by Entity P. Entity P wants to sell Entity A through an IPO using a Newco.



After

Newco issues new shares to acquire Entity A. Possibly Newco will raise new capital from public shareholders; however a period of several months may lapse.



Related IC topics—one business (2/2)

IC submission—2011

- The transaction in question is **not a BCUCC** because it **does not meet the definition of a 'business combination'**:
  - Newco cannot be identified as the acquirer according to IFRS 3.B18;
  - Entity A cannot be identified as the acquirer either, because Newco does not meet the definition of a business.
- The IC decided that this topic would be better considered within the context of a broader project on accounting for common control transactions and did not add the topic to its agenda.

2017 Board's clarification

The Board tentatively decided that the BCUCC project will address accounting for transactions under common control in which the reporting entity obtains control over one or more businesses, **regardless of whether IFRS 3 would identify the reporting entity** as the acquirer if IFRS 3 were applied.

According to the 2017 Board's clarification of the scope, the transaction discussed in the 2011 IC submission (slide 18) is included in the scope of the project.

Which financial statements? (1/2)

- **In 2014**, the Board **did not discuss which financial statements**—consolidated, separate or individual—the BCUCC project will focus on.
- **In 2017**, the Board decided that the **project will focus on the transactions** that the reporting entity needs to account for.

Which financial statements?

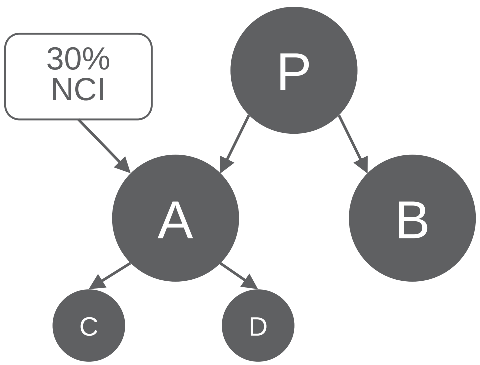
The scope will not specify **to which financial statements** of that reporting entity any accounting requirements developed in the project will apply.

This is because **the financial statements affected by any accounting requirements developed in the BCUCC project will depend on specifics of the transaction** *(see the example on next slide)*.

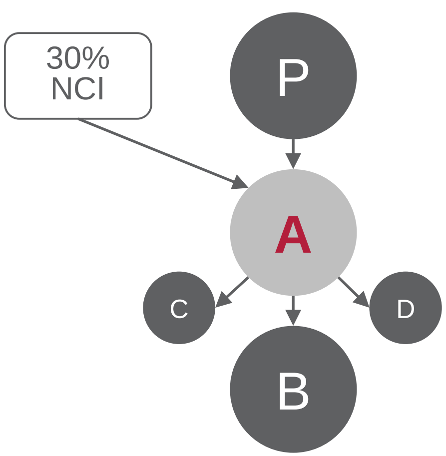
This is also **consistent with** how the scope is set out in **IFRS 3**.

Which financial statements? (2/2)

Transaction



Entity A acquires business B from Entity P.



B = separate entity

✓ **Any requirements developed in the BCUCC project will apply in Entity A consolidated financial statements.**

✓ **In Entity A separate financial statements, it will account for its investment in entity B applying IAS 27 *Separate Financial Statements*.**

B ≠ separate entity

✓ **Any requirements developed in the BCUCC project will apply in all financial statements prepared by Entity A (consolidated or separate).**

Clarifying the scope of the project

BCUCC

Description of BCUCC

- **BCUCC are business combinations in which all the combining entities or businesses are ultimately controlled by the same party or parties both before and after the business combination, and that control is not transitory (IFRS 3.B1).**

- The key components of this description are:

transaction is a ‘business combination’	**IFRS 3 defines ‘business combination’**	✓
all the combining entities are ‘under common control’	**IFRS 3.B2-B4 provide application guidance on how to assess ‘common control’**	✓
the common control is ‘not transitory’	**IFRS 3 does not elaborate on ‘transitory control’**	?

Business combinations vs BCUCC

Business combinations not under common control	BCUCC
IFRS 3 Acquisition method	No guidance Policy choice (IAS 8)

Application questions
(slides 25-27)

- Transitory control?
- Conditional IPO?
- …

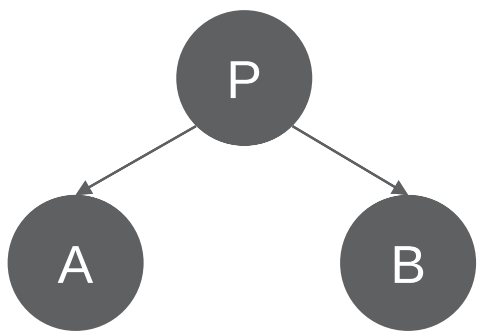
Related IC topics—transitory control (1/2)

IC submission—2006

- In **2006** the IC considered whether a **group restructuring involving a formation of a new entity** to facilitate the sale of a part of the group (eg in an IPO) is a business combination within the scope of IFRS 3.

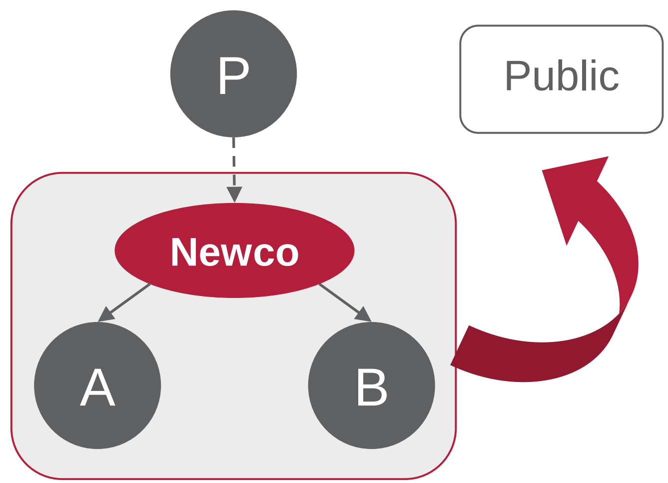
Before

Entity A and Entity B are controlled and fully owned by Entity P; Entity P wants to sell A and B through an IPO using a Newco.



After

In preparation of the IPO, Entity P formed a Newco and transferred Entity A and Entity B to that Newco.



Related IC topics—transitory control (2/2)

IC submission—2006

- Some argued that **control of the new entity is transitory** and therefore a combination involving a newly formed entity is a business combination within the scope of IFRS 3.
- The IC concluded that the consideration of common control applies to the **combining entities that existed before the combination, excluding the new entity**.
- The IC decided not to add this topic to its agenda.

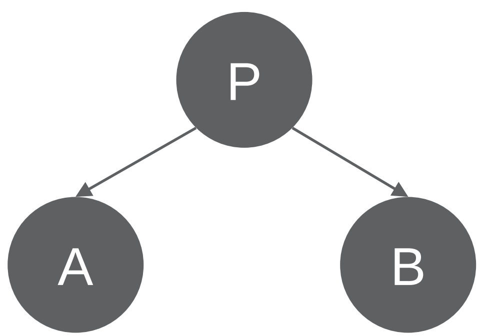
Related IC topics—conditional IPO (1/2)

IC submission—2011

- In **2011** the IC discussed a transaction where a newly formed entity (Newco) is established to acquire other entities under common control for cash raised in an IPO **and the acquisition is conditional on the occurrence of the IPO** (the IPO results in a loss of control of Newco).

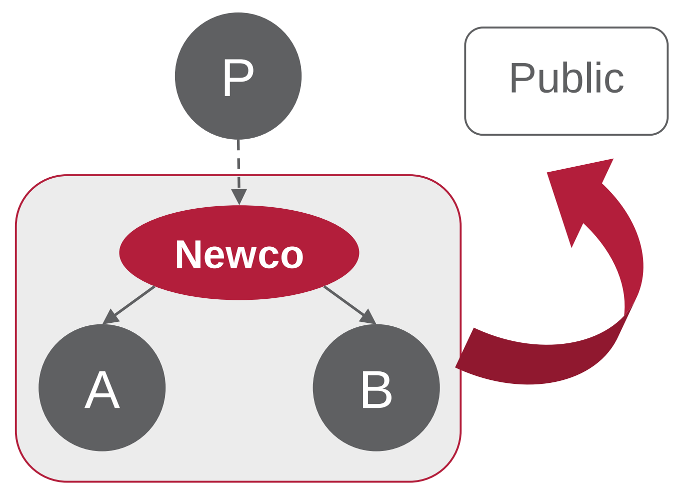
Before

Entity A and Entity B are controlled and fully owned by Entity P; Entity P wants to sell A and B through an IPO using a Newco.



After

Entity P formed a Newco.
Newco will acquire Entity A and B only on condition of the occurrence of Newco IPO.



Related IC topics—conditional IPO (2/2)

- Regarding the example on the previous slide:
  - ❶ some argue that **the IPO takes place before the acquisition**, hence Entity P does not control Newco at the time of the acquisition, therefore **the acquisition is NOT a BCUCC**;
  - ❷ others argue the **acquisition happens before the IPO**. This would mean that Entity P controls Newco, Entity A and B at the time of the acquisition. However, there are **different views as to whether Entity P's control** over Newco, Entity A and Entity B **is transitory**:
    - if **YES—transitory control** ➲ **NOT a BCUCC**
    - if **NOT—control not transitory** ➲ **BCUCC**
- The IC decided that this topic would be better considered within the context of a broader project on accounting for common control transactions and did not add the topic to its agenda.

Staff recommendation

Application questions focus on the distinction between BC and BCUCC…

Business Combinations
not under common control

BCUCC

Application questions

Acquisition method

Different method(s)

Staff recommendation on scope of BCUCC project

'Fill in the gap' in accounting for business combinations, instead of focussing on the distinction between BC and BCUCC.

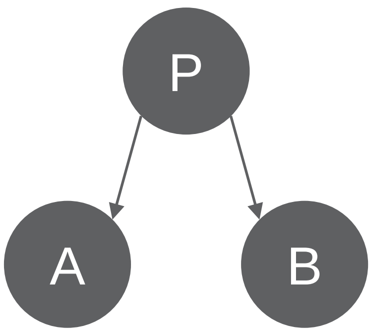
Illustrations of transactions within the scope

Example 1—Basic

Before

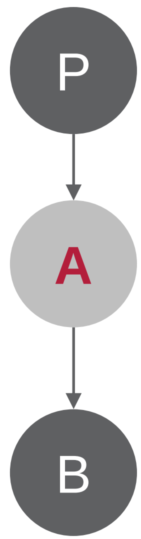
Entity A and Entity B are controlled by Entity P.

Entity B is a business.



After

Entity A acquires Entity B.



Focus on A's perspective

Observations

Covered by BCUCC project, regardless of whether the combining parties:

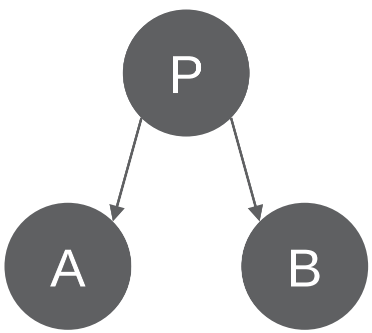
- are fully owned by Entity P or there is NCI in the combining parties;
- are listed or privately held; or
- are preparing for an IPO.

Example 2—Newco

Before

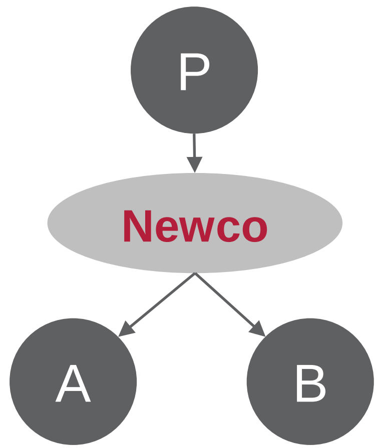
Entity A and Entity B are controlled by Entity P.

Both Entity A and Entity B are businesses.



After

Entity P forms a Newco and transfers Entity A and Entity B to that Newco.



Focus on Newco's perspective

Observations

Covered by BCUCC project, regardless of whether:

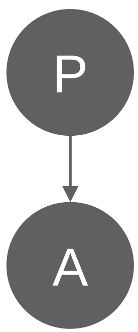
- ✓ Newco can be identified as the 'acquirer' if IFRS 3 were applied to the transaction; and
- ✓ the combining parties:
  - are fully owned by Entity P or there is NCI in the combining parties;
  - are listed or privately held; or
  - are preparing for an IPO.

Example 3—One business

Before

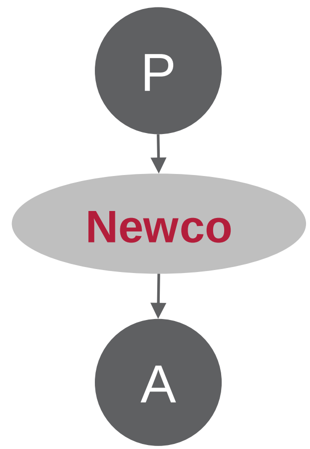
Entity A is controlled by Entity P.

Entity A is a business.



After

Entity P forms a Newco and transfers Entity A to that Newco.



Focus on Newco's perspective

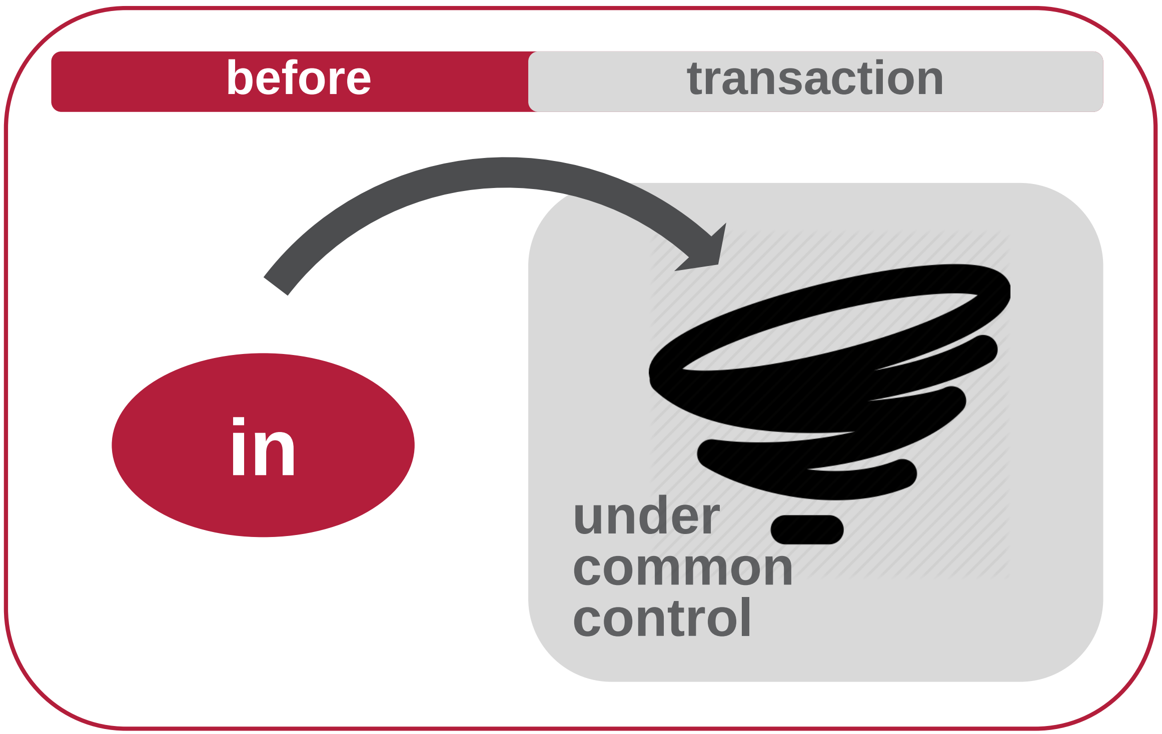
Observations

Covered by BCUCC project, regardless of whether:

- ✓ Newco can be identified as the 'acquirer' if IFRS 3 were applied to the transaction; and
- ✓ the combining parties:
  - are fully owned by Entity P or there is NCI in the combining parties;
  - are listed or privately held; or
  - are preparing for an IPO.

Transitory control—Situation A

Staff recommendation

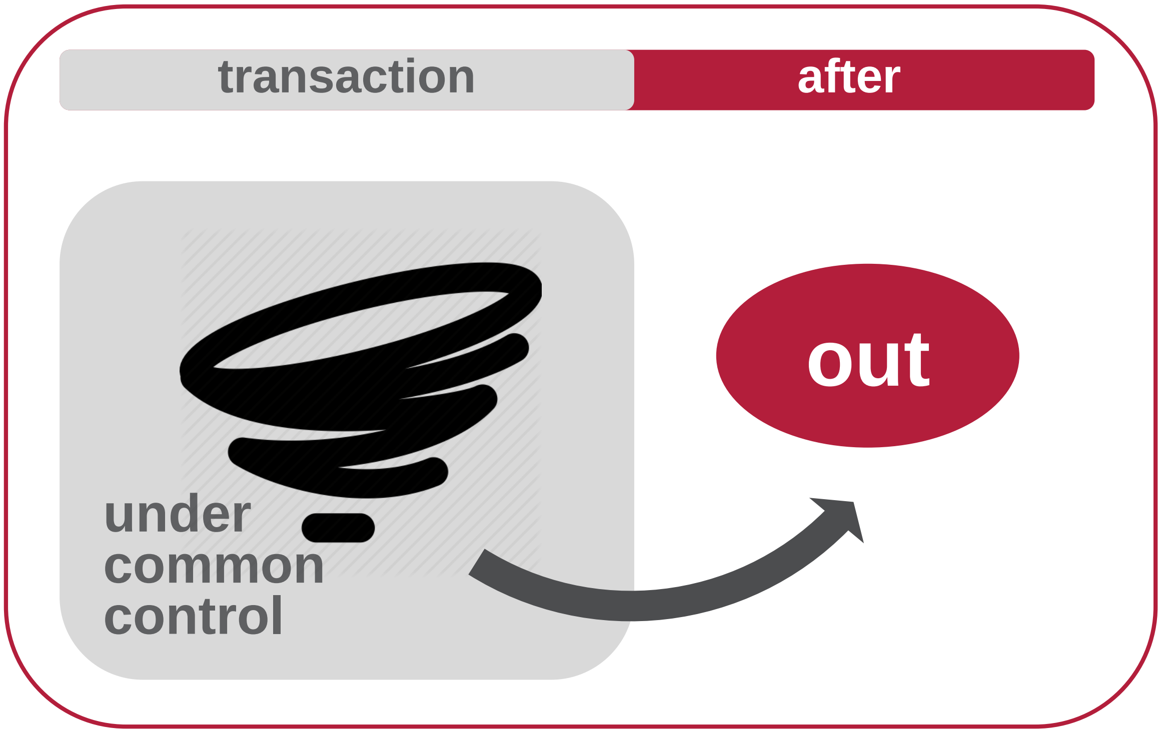


‘Fill in the gap’ in accounting for business combinations, instead of focusing on the distinction between BC and BCUCC

Transactions preceded by an external acquisition
will be covered by the BCUCC project

Transitory control—Situation B

Staff recommendation



‘Fill in the gap’ in accounting for business combinations, instead of focusing on the distinction between BC and BCUCC

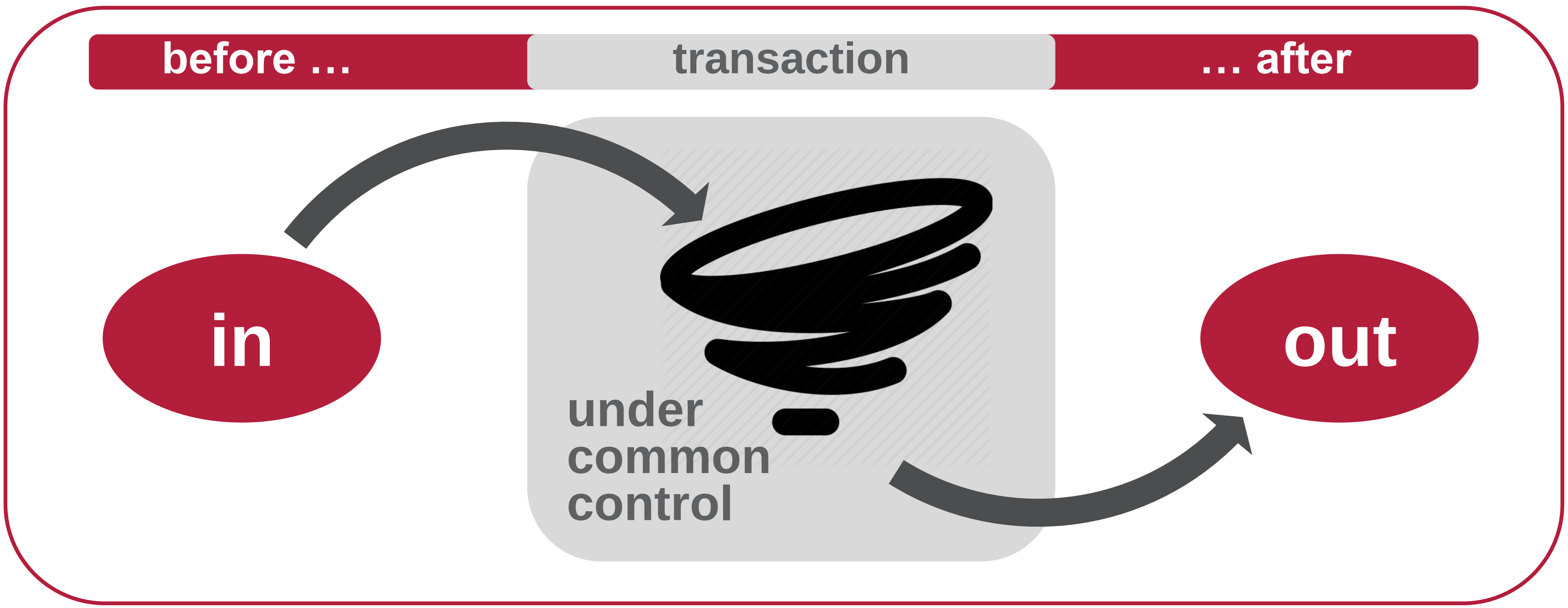
Transactions followed by an external sale, including those conditional on IPO, will be covered by the BCUCC project

Transitory control—Situation C

Staff recommendation

‘Fill in the gap’ in accounting for business combinations,
instead of focusing on the distinction between BC and BCUCC

Transactions preceded by an external acquisition *and* followed by an external sale
will be covered by the BCUCC project



Discussion

Discussion

Your views on the scope of the project

- Do you agree with the proposed scope of the project? If not, why?
- Are there any other transactions or perspectives that the Board should consider? If yes, what other transactions or perspectives and why?

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