Staff paper

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IASB® meeting

Date	**September 2023**
Project	**Business Combinations under Common Control**
Topic	**Due Process Handbook assessment**
Contacts	Richard Brown (rbrown@ifrs.org) Zicheng Wang (zwang@ifrs.org)

Introduction and purpose

1. As Agenda Paper 23 explains:

   (a) Agenda Paper 23A summarises and analyses feedback on whether the International Accounting Standards Board (IASB) should:

      (i) choose Option I (develop recognition, measurement and disclosure requirements);[1] or

      (ii) change project direction—that is, choose Option II (develop disclosure-only requirements) or Option III (discontinue the project);

   (b) Agenda Paper 23B summarises and analyses feedback on what the IASB should do if it changes project direction—that is, whether to choose Option II or Option III; and

   (c) this paper provides an updated assessment of the Due Process Handbook requirements for a standard-setting project (taking into account stakeholders' feedback and our analysis of that feedback) and explains our initial views on

[1] As paragraph A4 explains, if the IASB chooses Option I it would then need to decide which specific recognition, measurement and disclosure requirements to develop, which might differ from the preliminary views in the Discussion Paper *Business Combinations under Common Control*.

whether to change project direction and, if so, whether to choose Option II or Option III.

2. This paper does not ask the IASB for decisions.

Overview and structure

3. This paper covers:

(a) Due Process Handbook requirements (paragraphs 4–32) including:

(i) criteria for potential standard-setting projects (paragraphs 6–25); and

(ii) the IASB's resources (paragraphs 26–32);

(b) staff initial views (paragraphs 33–36);

(c) next steps (paragraphs 37–38);

(d) questions for the IASB; and

(e) Appendix A—Illustration of the options.

Due Process Handbook requirements

4. As paragraph 20 of Agenda Paper 23A of the IASB's April 2023 meeting explains:

(a) the Due Process Handbook includes requirements the IASB assesses when moving a project from the research phase into the standard-setting phase; and

(b) by assessing those requirements we can consider whether the project is likely to move into the standard-setting phase in future.

5. Paragraphs 5.1–5.7 of the Due Process Handbook require the IASB to assess:

(a) criteria for potential standard-setting projects (paragraphs 6–25); and

(b) the IASB's resources (paragraphs 26–32).

Criteria for potential standard-setting projects

6. Paragraph 5.4 of the Due Process Handbook explains:

> The [IASB] evaluates the merits of adding a potential project to the work plan primarily on the basis of the needs of users of financial reports, while also taking into account the costs of preparing the information in financial reports. When deciding whether a proposed agenda item will address users' needs, the [IASB] considers:
>
> (a) whether there is a deficiency in the way particular types of transactions or activities are reported in financial reports;
>
> (b) the importance of the matter to those who use financial reports;
>
> (c) the types of entities likely to be affected by any proposals, including whether the matter is more prevalent in some jurisdictions than others; and
>
> (d) how pervasive or acute a particular financial reporting issue is likely to be for entities.

7. Taking into account stakeholders' feedback and our analysis of that feedback, paragraphs 8–25 include our assessment of these criteria in the context of the business combinations under common control (BCUCCs) project.

Deficiency in reporting

What is the deficiency in reporting?

8. The scope of IFRS 3 *Business Combinations* excludes BCUCCs, which is a 'gap' in IFRS Accounting Standards. Paragraphs 9–14 consider the extent to which the 'gap' in IFRS Accounting Standards causes a deficiency in reporting for BCUCCs.

9. Considering feedback from stakeholders in developing the Discussion Paper *Business Combinations under Common Control*, the IASB set a project objective which is to develop reporting requirements for a receiving entity that would reduce diversity and improve the transparency of reporting BCUCCs. More specifically, the IASB aims to provide users of a receiving entity's financial statements with better information that is both:

   (a) more relevant—by setting up reporting requirements based on user information needs; and

   (b) more comparable—by requiring similar transactions to be reported in a similar way.

10. Consistent with the project objective, we think there is a deficiency in reporting BCUCCs because:

   (a) there is diversity in recognising and measuring BCUCCs (paragraphs 7–12 of Agenda Paper 23A);

   (b) there is diversity in disclosure of information about BCUCCs (paragraphs 9–13 of Agenda Paper 23B); and

   (c) users could receive more relevant information than they typically receive today—for example:

      (i) 94% of BCUCCs by publicly traded entities (which typically affect the entity's non-controlling shareholders (NCS)) in our 2019 research were accounted for applying a form of book-value method;[2] but

      (ii) as Agenda Paper 23E of the IASB's November 2022 meeting explains, our initial view after considering feedback on the Discussion Paper was that the acquisition method would meet users' common information needs for a BCUCC that affects NCS better than a book-value method.

[2] For our 2019 research see Appendix C of Agenda Paper 23B of the IASB's February 2020 meeting.

What are the consequences of the deficiency in reporting?

11. The deficiency in reporting BCUCCs may not have significant consequences because:

    (a) diversity in recognising and measuring BCUCCs may not be extensive because, for example:

        (i) of local requirements or practice being largely settled (paragraph 9(a) of Agenda Paper 23A); or

        (ii) auditors, preparers and regulators engage with each other to debate and agree the appropriate reporting for a BCUCC;[3]

    (b) some users said they could work with diversity in recognising and measuring BCUCCs (paragraph 20(a) of Agenda Paper 23A), suggesting that such diversity is not significantly affecting their decision-making; and

    (c) the lack of specific examples of reporting for BCUCCs which can be described as 'misleading' (paragraphs 47–50 of Agenda Paper 23A) suggests that significant deficiencies in reporting BCUCCs are rare.

To what extent would the options address the deficiency in reporting?

12. Only Option I could address diversity in recognising and measuring BCUCCs. There is a risk that Option II could increase diversity in recognising and measuring BCUCCs. By completing a project which only develops disclosure requirements for BCUCCs, there is a risk that stakeholders interpret the IASB's decision to not develop recognition and measurement requirements as permitting a policy choice of how to recognise and measure BCUCCs. To mitigate this risk, the IASB could explain its reasons for not developing recognition and measurement requirements in the Basis for Conclusions of the disclosure requirements it develops.

13. Although Option II would not reduce diversity in recognising and measuring BCUCCs, it could partially address the deficiency in reporting by:

[3] Stakeholders reported that they incur costs engaging with each other (see paragraph 13 of Agenda Paper 23A) which is considered alongside the resources required for Option I in paragraph 29.

(a) reducing diversity in disclosure of information about BCUCCs (paragraph 12 of Agenda Paper 23B explains that our 2019 research indicates that the information disclosed about BCUCCs appears to be inconsistent); and

(b) providing users with more relevant information than they typically receive today (for example, paragraph 26 of Agenda Paper 23A explains that we think disclosure of fair value information could partially meet users' information needs for a BCUCC that affects NCS).[4]

14. Option III would not address the deficiency in reporting to any extent, because the IASB would not develop any requirements for reporting BCUCCs.

Importance to users

15. As paragraphs 34–36 of Agenda Paper 23A explain, we think:

(a) the fact that most users said to change project direction indicates they do not prioritise Option I; but

(b) many other stakeholders prioritise Option I which could be explained, for example, by stakeholders' engagement with entities that undertake BCUCCs differing.

16. As paragraph 44–46 of Agenda Paper 23A explains, jurisdictional diversity in user feedback for BCUCCs that affect NCS means that Option I may be less important to users than originally anticipated because:

(a) requiring a single method to be applied would likely not meet the information needs reported by all users; and

(b) allowing entities to choose which method to apply might not change reporting practice for BCUCCs.

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[4] As paragraph 7 of Agenda Paper 23B explains, the IASB has not yet discussed what a disclosure-only project would cover if the IASB chooses Option II.

17. The fact that most users suggested choosing Option II over Option III indicates that they do prioritise a disclosure-only project. However, some users preferred Option III with a few users saying the project is a low priority.

Types of entities likely to be affected

18. The project would affect any receiving entity that enters into a BCUCC. However, a BCUCC can occur only if the reporting entity and other businesses are under common control. A publicly traded entity with disperse ownership and no controlling party cannot be a receiving entity in a BCUCC but entities which are under common control (for example, subsidiaries within a group) can undertake BCUCCs.

19. Paragraphs 40–41 of Agenda Paper 23A explain that stakeholders reported split views on the frequency of BCUCCs which we think might suggest:

    (a) BCUCCs by publicly traded entities (which many users often focus on) may be rare;

    (b) BCUCCs by privately held entities (covered by national standard-setters) may be common; and

    (c) BCUCCs in preparation for a capital market transaction such as an initial public offering (covered by regulators) may be common.

20. As paragraph 45 of Agenda Paper 23A explains, our 2019 research suggests that BCUCCs by publicly traded entities (which typically affect NCS) are more prevalent in China than in other jurisdictions.[5]

How pervasive or acute the issue is likely to be

21. The preliminary views in the Discussion Paper were that in principle, the acquisition method should apply to BCUCCs that affect NCS and a book-value method should

[5] The footnotes to paragraphs 32 and 34 of Agenda Paper 23A of the IASB's April 2023 meeting explain research limitations and assumptions.

apply to BCUCCs that do not affect NCS. We analyse how pervasive or acute the change in the measurement method would be separately for BCUCCs that affect NCS (paragraphs 22–23) and BCUCCs that do not affect NCS (paragraphs 24–25).

BCUCCs that affect NCS

22. We are not aware of BCUCCs that affect NCS being common across jurisdictions, particularly BCUCCs by publicly traded entities (which we expect to typically affect NCS). As paragraph 45 of Agenda Paper 23A explains, 52% of these transactions in our 2019 research were by entities listed in a single jurisdiction.

23. Ninety-four per cent of the BCUCCs in our 2019 research were accounted for applying a form of book-value method. If the IASB chooses Option I and requires entities to apply the acquisition method to BCUCCs that affect NCS (in line with the preliminary views in the Discussion Paper), the measurement method applied for reporting most BCUCCs that affect NCS would change.[6]

BCUCCs that do not affect NCS

24. As paragraph 21 explains, we think BCUCCs by privately held entities or in anticipation of a capital market transaction (which we expect to typically not affect NCS) are more common than BCUCCs that affect NCS.

25. We understand that a form of book-value method is typically (but not always) applied to BCUCCs that do not affect NCS. If the IASB chooses Option I and requires entities to apply a book-value method to BCUCCs that do not affect NCS (in line with the preliminary views in the Discussion Paper), the IASB would:

    (a) standardise this practice and provide clarity to stakeholders (such as preparers, auditors and regulators); but

    (b) likely not significantly change practice given our understanding that a book-value method is typically applied today.

[6] As paragraph A4 explains, the IASB could choose Option I but then develop other requirements.

The IASB's resources

26. Paragraph 5.7 of the Due Process Handbook explains that the IASB adds a standard-setting project to the work plan only if it concludes that the benefits of the improvements to financial reporting will outweigh the costs. As well as the IASB expending its own resources, the IASB's stakeholders expend resources, including when, for example:

    (a) reviewing consultation documents and submitting comment letters; and

    (b) participating in fieldwork.

27. The magnitude of the project (and therefore resources required) to develop an exposure draft and finalise an IFRS Accounting Standard will depend on various factors including what requirements the IASB develops. Appendix A illustrates potential Due Process milestones and the resources that would be necessary for each of the three options.

Resources required for Option I

28. Option I would require significant resources to develop an exposure draft and finalise an IFRS Accounting Standard. Although the IASB already reached preliminary views in its Discussion Paper, to develop an exposure draft the IASB would need to:

    (a) deliberate all the workstreams illustrated in Appendix A, including topics on which respondents to the Discussion Paper had mixed views (see paragraph 51 of Agenda Paper 23A) which may require further research or outreach; and

    (b) develop proposals more detailed than the Discussion Paper—for example, addressing situations such as book values not being readily available.

29. As Appendix A illustrates, Option I would require significantly more resources than Option II or Option III. However, considering resources more widely, as paragraph 13 of Agenda Paper 23A explains, stakeholders (such as preparers) incur costs as a result

of IFRS Accounting Standards not containing requirements for BCUCCs and only Option I would reduce these ongoing costs.

30. Paragraph B4(d) of Agenda Paper 23A explains that a few respondents suggested limiting the scope of any recognition and measurement requirements the IASB develops by reducing the scope of BCUCCs covered by the project, or by developing recognition and measurement requirements for only some of the workstreams. Whilst these suggestions would reduce the resources required, they would also reduce the benefits of choosing Option I so we think they do not significantly change the assessment of whether the benefits of Option I would justify the resources necessary.

Resources required for Option II

31. As Appendix A illustrates, Option II would require significantly less resources than Option I. The resources required will depend on what requirements the IASB develops, including whether the objective would be to:

    (a) improve transparency of accounting policies applied to recognise and measure BCUCCs—for example, which measurement method is applied;

    (b) improve transparency about BCUCCs recognised in the financial statements—for example, the recognised amounts of each class of assets received and liabilities assumed; and/or

    (c) provide relevant information in addition to transparency of what is recognised in financial statements in relation to a BCUCC—for example, requiring entities that apply a book-value method to recognise and measure a BCUCC that affects NCS to disclose selected fair value information.

32. As a starting point for developing disclosure requirements, the IASB could leverage existing requirements in IFRS 3 (including amendments arising from the IASB's *Business Combinations—Disclosure, Goodwill and Impairment* project) and consider feedback on the preliminary views in the Discussion Paper related to disclosure requirements. The IASB could also consider how to design a disclosure-only project

to minimise the resources needed. However, some resources would be necessary to adapt existing requirements to be compatible with diversity in recognising and measuring BCUCCs.

Staff initial views

Whether to change project direction

33. We agree with stakeholders that Option I would improve the reporting for BCUCCs and only Option I could reduce diversity in recognising and measuring BCUCCs. However, if the IASB chooses Option I, a major decision would be whether to develop:

    (a) prescriptive recognition and measurement requirements—for example, similar to the preliminary views in the Discussion Paper or requiring an entity to apply a book-value method to all BCUCCs—which would:

        (i) reduce diversity in recognising and measuring BCUCCs; but

        (ii) due to jurisdictional diversity in user feedback, not meet the information needs reported by all users; or

    (b) less prescriptive recognition and measurement requirements—for example, allowing entities to choose which method to apply to some or all BCUCCs—which would:

        (i) not reduce diversity in recognising and measuring BCUCCs; and

        (ii) due to jurisdictional diversity in user feedback, not always fully meet user information needs—for example, if an entity has users that prefer different methods.

34. In our initial view, considering stakeholder feedback and the Due Process Handbook requirements analysed in paragraphs 4–32, we think the benefits of choosing Option I

would not justify the resources necessary. Consequently, we think the IASB should change project direction. In particular:

(a) most users suggested changing project direction indicating the project is not a priority for most users;

(b) the deficiency in reporting may not have significant consequences;

(c) irrespective of whether the IASB chooses to develop prescriptive (or less prescriptive) requirements, jurisdictional diversity in user feedback means those requirements will not always fully meet users' information needs so the project would not achieve the original objective; and

(d) Option I would incur significant resources.

Whether to choose Option II or Option III

35. Most stakeholders (including most users) who expressed a preference between Option II or Option III supported Option II. Although neither Option II nor Option III would reduce diversity in recognising and measuring BCUCCs, Option II could reduce diversity in disclosure of information about BCUCCs and provide users with more relevant information than they typically receive today.

36. The IASB has not yet discussed what a disclosure-only project would cover if the IASB chooses Option II. We have therefore not reached an initial view about whether the benefits of Option II would justify the resources necessary and whether to choose Option II or Option III. We think that, before deciding whether to choose Option II or Option III, the IASB should have an initial discussion in an upcoming meeting to consider what a disclosure-only project could cover.

Next steps

37. In a future IASB meeting we expect to present:

(a) an overview of what a disclosure-only project could cover, for example:

(i) explaining the potential main decisions the IASB would need to make (see paragraph A10); and

(ii) the extent of further consultation and outreach that would be necessary to make those decisions and develop an exposure draft;

(b) analysis of whether the benefits of choosing Option II would justify the resources necessary;

(c) updated analysis, for example, if IASB members asked for further analysis of matters included in the agenda papers for this meeting; and

(d) our recommendations, and ask the IASB to decide:

(i) whether to change project direction; and

(ii) if the IASB decides to change direction, whether to choose Option II or Option III.

38. The overview of what a disclosure-only project could cover would aim to provide a sufficient overview for the IASB to decide whether to choose Option II. This overview would not analyse all aspects of a disclosure-only project in detail, to avoid investing resources before the IASB decides whether to explore a disclosure-only project. As Appendix A explains, if the IASB chooses Option II and changes project direction to developing disclosure-only requirements, the IASB might still later decide that the project should not move into the standard-setting phase.

Questions for the IASB

1) Do IASB members have comments or questions on:

(a) the feedback and analysis in Agenda Papers 23A and 23B?

(b) our assessment of the Due Process Handbook requirements in this agenda paper?

2) For the next steps explained in paragraphs 37–38:

(a) do IASB members have any questions on our suggested next steps?

(b) is there anything IASB members would like us to research or analyse further before the IASB decides on project direction in a future meeting?

Questions for the IASB
3) Do IASB members have any other comments or questions?

Appendix A—Illustration of the options

A1. This appendix illustrates potential Due Process milestones and resources required if the IASB chooses each of the three options. This illustration is intended to support our assessment of the Due Process Handbook requirements and specifically whether the benefits of choosing Option I or Option II would justify the resources necessary, assessed in paragraphs 26–32.

A2. For illustration we assume that Option I and Option II would lead to the issuance of an IFRS Accounting Standard (Accounting Standard)[7] but:

(a) the IASB might choose Option I or Option II but later decide that the project should not move into the standard-setting phase; and

(b) the IASB might move the project into the standard-setting phase but not issue an Accounting Standard—for example, after considering feedback on an exposure draft the IASB might decide not to proceed with the project.

Option I—develop recognition, measurement and disclosure requirements

A3. If the IASB chooses Option I, the project would continue with the current objective (paragraph 9).

A4. The IASB would continue deliberating recognition, measurement and disclosure requirements. The IASB would consider feedback on the Discussion Paper when developing requirements. These requirements might differ from the preliminary views in the Discussion Paper.

A5. The resources required will depend on the IASB's decisions—for example, if the IASB allows entities to choose which measurement method to apply to all BCUCCs then it might not need to deliberate exceptions. For illustration, we assume that the

[7] For simplicity, this Appendix refers to issuance of an IFRS Accounting Standard but the IASB could decide to amend an existing IFRS Accounting Standard.

IASB proposes requirements broadly in line with its preliminary views in the Discussion Paper.

Due Process milestones

A6. Assuming the project leads to the issuance of an Accounting Standard, the IASB would publish an exposure draft and issue a final Accounting Standard containing recognition, measurement and disclosure requirements.

Resources required

A7. Assuming the IASB proposes requirements broadly in line with its preliminary views in the Discussion Paper (see paragraph A5), the topics we expect to be the most resource-intensive are:

(a) scope:

   (i) whether to cover group restructurings and if so how to define them;[8] and

   (ii) transitory common control;[9]

(b) selecting the measurement method:

   (i) which method(s) to apply in principle;

   (ii) exceptions, including exploring possible new exceptions in more detail; and

   (iii) clarification requests / application guidance to make the principle and any exceptions workable;

(c) applying the acquisition method:

[8] The preliminary view in the Discussion Paper was to consider group restructurings (transactions that involve a transfer of a business under common control but do not meet the definition of a 'business combination' in Appendix A of IFRS 3).

[9] In describing BCUCCs, IFRS 3 requires that common control is 'not transitory' but does not provide guidance on that notion. The preliminary view in the Discussion Paper was to develop proposals that cover transactions preceded by an acquisition from an external party or followed by (or conditional on) a sale of the combining companies to an external party.

(i) special features for distributions from / contributions to the receiving entity's equity; and

(ii) disclosure requirements; and

(d) applying a book-value method:

(i) whether to:

1. prescribe one standardised book-value method;

2. prescribe different book value-methods for different circumstances; or

3. allow entities a choice of how to apply a book-value method;

(ii) which book values to use, addressing situations such as:

1. book values not being readily available;

2. differing accounting policies; and

3. whether a BCUCC results in the initial recognition of assets and liabilities or whether the assets and liabilities would retain any associated history (for example, classification of financial instruments);

(iii) whether to restate pre-combination information;

(iv) disclosure requirements; and

(v) clarification requests / application guidance to make the requirements workable.

Option II—develop disclosure-only requirements

A8. If the IASB chooses Option II, it would need to update the project objective because the project would not reduce diversity in recognising and measuring BCUCCs. The IASB would need to decide on the project objective, but the project objective could, for example, be to:

(a) improve transparency of the accounting policies applied to recognise and measure BCUCCs—for example, which measurement method is applied;

(b) improve transparency about BCUCCs recognised in the financial statements—for example, the recognised amounts of each class of assets received and liabilities assumed; and/or

(c) provide relevant information in addition to transparency of what is recognised in the financial statements in relation to a BCUCC—for example, requiring entities that apply a book-value method to recognise and measure a BCUCC that affects NCS to disclose selected fair value information.

Due Process milestones

A9. If the IASB chooses Option II, the IASB would publish an exposure draft and issue a final Accounting Standard containing only disclosure requirements. These requirements would not address how to recognise and measure BCUCCs and would only contain requirements to disclose information about BCUCCs.

Resources required

A10. The resources required will depend on the requirements that the IASB develops. The IASB has not yet discussed what a disclosure-only project would cover if the IASB chooses Option II but potential main decisions to deliberate include:

(a) the objective of a disclosure-only project (see paragraph A8);

(b) whether the same disclosure requirements should apply to all BCUCCs or, for example:

(i) whether to require entities that apply the acquisition method to a BCUCC to apply IFRS 3's disclosure requirements; and/or

(ii) whether any disclosure requirements developed in this project should only apply to specified BCUCCs—for example, whether to only require entities to disclose fair value information for BCUCCs that affect NCS; and

(c) the approach to developing disclosure requirements—for example, whether to primarily focus on leveraging (and adapting if necessary) existing disclosure requirements in IFRS 3 or consider developing a new set of requirements.

Option III—develop no recognition, measurement or disclosure requirements

Due Process milestones

A11. The IASB could choose to not develop any reporting requirements for BCUCCs so would discontinue the project and not publish any Due Process documents.

Resources required

A12. If the IASB chooses Option III, it would not require significant additional resources. Some resources may be needed as a consequence of discontinuing the project—for example, to prepare a project summary report.