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Business Combinations under Common Control

Cover Note

Objective

- 1 The objective of the session is to discuss project direction options in preparation for the July ASAF meeting.
- 2 The questions for EFRAG FR TEG-CFSS members are included in agenda paper 07-02.

Background

- 3 In November 2020, the IASB published its [Discussion Paper DP/2020/2 Business Combination under Common Control](#) ('the DP') with a comment period ending on 1 September 2021. EFRAG published its [CL](#) on 8 October 2021.
- 4 In [December 2021](#) and [January 2022](#), the IASB considered feedback on the DP and discussed a deliberation plan starting with the project scope and selecting the measurement method.
- 5 In [March 2022](#), the IASB deliberated the objective and scope of the project and tentatively decided:
 - (a) to update the project's objective to reflect the stage of the project and to emphasise that the DP considers the needs of users of the receiving entity's (that is, the reporting entity's) financial statements; and
 - (b) **not to expand** the project's scope with:
 - (i) reporting by other entities;
 - (ii) reporting for an investment in a subsidiary received under common control in the separate financial statements; or
 - (iii) reporting of other common control transactions;
 - (c) the IASB has not yet made tentative decisions about other aspects such as group restructurings or transitory control.
- 6 Starting from June 2022, the IASB started redeliberating its preliminary views on selecting the measurement method to apply to BCUCCs. The IASB was not asked to make any decisions. In particular, the IASB discussed:
 - (a) whether conceptually the acquisition method and/or a book-value method should apply to business combinations under common control (e.g., the similarities and differences between BCUCC and business combinations covered by IFRS 3 *Business Combinations* and the types of users of a receiving entity's financial statements and their information needs compared to those of a business combination covered by IFRS 3) – [IASB Update June 2022](#);

- (b) the principle for selecting which measurement method a receiving entity would apply to a business combination under common control – [IASB Update November 2022](#) and [December ASAF meeting summary](#); and
 - (c) whether in some circumstances—including those described in the DP—a receiving entity would be permitted or required to deviate from the principle and apply a different measurement method (e.g., the optional exemption, the related-party exception, a criterion for publicly traded shares and other possible exceptions, including those for government-related entities or insignificant NCS) – [IASB Update November 2022](#) and [December ASAF meeting summary](#).
- 7 At its November 2022 meeting, the IASB also identified four areas to research further before making decisions on selecting the measurement method:
- (a) what proportion of BCUCCs affect NCS compared with BCUCCs that do not affect NCS;
 - (b) whether a receiving entity should have an option to apply the acquisition method to BCUCCs that do not affect NCS;
 - (c) more details on a possible exception for insignificant NCS; and
 - (d) in the context of the related party exception, whether related parties which are not part of the common control group (for example, associates) rely on general purpose financial statements to meet their information needs.
- 8 On these areas, the IASB Staff consulted the Emerging Economies Group ([EEG](#)) and the Accounting Standards Advisory Forum ([ASAF](#)) at their December 2022 meetings. EEG and ASAF members expressed different views on both the principle for selecting the measurement method and exceptions. EEG and ASAF members also suggested clarifications to make the IASB’s initial views more operational.
- 9 A summary of the most recent EFRAG discussions can be found in the Appendix.

Latest developments

- 10 In its [April 2023](#) meeting the IASB considered the direction of its project on BCUCC. At this meeting, the IASB did not address the aforementioned four areas because it is considering the project direction first. After the IASB decides the project direction, it will address these areas in future IASB meetings if relevant. The IASB was not asked to make any decisions. The IASB will seek feedback from its consultative groups before continuing its discussions. For example, the project was discussed at the Capital Markets Advisory Committee and Global Preparers Forum in June.
- 11 The IASB discussed whether the merits of continuing in the current direction are likely to justify the necessary resources or whether to consider changing the direction.
- 12 Please refer to the Agenda Paper 07-02 for further information on the IASB meeting held in April.
- 13 To gather more information to help the IASB make an informed decision on project direction the topic will be discussed at the July ASAF meeting. Please refer to the ASAF agenda papers attached in 07-03, 07-04 and 07-05 (for background only).

Next steps

- 14 This topic on project direction will be discussed at the EFRAG User Panel on 12 July and at the EFRAG FRB meeting on 13 July.
- 15 The EFRAG Secretariat will continue to monitor the IASB’s discussions.

Agenda Papers

- 16 In addition to this cover note, agenda papers for this session are:
- (a) Agenda paper 07-02 – *BCUCC Issues paper Update on the IASB discussions*
 - (b) Agenda paper 07-03 - *AP5-bcucc-cover-paper* (ASAF paper) - (for background only)
 - (c) Agenda paper 07-04 - *AP5a-bcucc-project-direction* (ASAF paper) - (for background only)
 - (d) Agenda paper 07-05 - *AP5b-bcucc-project-direction-bvm* (ASAF paper) - (for background only)

Appendix: The most recent EFRAG discussions

EFRAG previous discussions

- 1 At the November 2022 EFRAG FR TEG-CFSS and January 2023 EFRAG FR TEG meetings, members discussed the IASB's initial views on the principles of selecting the measurement method to apply to a BCUCC and the application of exceptions or exemptions when selecting the measurement method. A summary of the discussions is provided below.

EFRAG FR TEG-CFSS meeting held in November

- 2 EFRAG FR TEG-CFSS were provided an update on the BCUCC project and were asked for their views on particular aspects of selecting the measurement method(s) to apply to BCUCCs.
- 3 Consistent with the view in EFRAG CL, many members indicated that the economic substance should be the key element in selecting the measurement model. Although it was a rules-based approach, the IASB's preliminary views included in paragraph 2.55 of the DP would offer an acceptable compromise mainly due to practical consideration. Furthermore, some members supported the IASB's approach for example because assessing the economic substance is too judgemental and on cost-benefit grounds.
- 4 One member commented that BCUCCs were unique transactions and achieving comparability across these types of transactions was not justified. It was acknowledged that reflecting the economic substance would result in a trade-off between comparability and relevance of information.
- 5 One member did not support the principle that the acquisition method should be applied if NCS is affected. Indeed, there could be situations where NCS is not involved but the acquisition method would be more appropriate or NCS is affected but the book-value method would be more appropriate. It was not also clear if the receiving entity was a Newco or just a restructuring how the proposed measurement methods would be applied to the BCUCC.
- 6 If the IASB continued the way that was being proposed, then there was support for the insignificant NCS exception. Regarding insignificant NCS:
 - (a) some type of guidance was welcome on what insignificant NCS means. If we think about significant influence 20% appears to be rather high. In many jurisdictions 10% of minority is a relevant threshold to trigger rights to redeem at fair value. However, even a threshold of 10% was still seen to be rather high;
 - (b) furthermore, members did not support establishing a quantitative threshold for determining insignificant NCS.
- 7 Regarding the government-related entities exception, members, in general, either questioned whether there should be an exception for this or did not agree with this exception. They were also not convinced by the conceptual reasons for having this exception. In case of listed companies, the government exception did not make much sense.
- 8 Further comments included:
 - (a) it was not clear how the different exceptions in the packages interact with each other; and
 - (b) EFRAG had recommended in its comment letter to consider the interests of other stakeholders, like lenders and other creditors, when determining the measurement method. One member indicated that lenders are not in favour of the acquisition method as this improves the leverage. Another member indicated that the IASB staff, in their November IASB Staff paper, the information provided by either the

acquisition method or a book-value method could meet lenders and other creditors' information needs.

EFRAG FR TEG meeting held in January 2023

- 9 EFRAG FR TEG discussed the November 2022 IASB discussions and the December 2022 ASAF discussions on the BCUCC project. The discussions related to the principle of selecting the measurement method for BCUCCs, and exemptions and exceptions to apply a different method as a result of the cost-benefit trade-off and other practical considerations.
- 10 On the suggested option to apply the acquisition method for BCUCCs that do not affect NCS (the “NCS choice” principle):
 - (a) A few members were not supportive of this proposal. The reasons provided by them included that the purpose of the project is to reduce diversity in practice in accounting for such transactions and would be against the project objective and the option would not help with comparability.
 - (b) One member considered that most of the companies would apply the book value method as it would, for example, be less costly than the acquisition method, therefore, this member would question why the entity would choose to apply the acquisition method.
- 11 Another member preferred having a different starting point that all BCUCCs should be at fair value and then to have some exceptions.