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Paper 10-02
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Update on BCUCC developments
Issues Paper

Objective

1 The purpose of this paper is to update EFRAG TEG on the IASB's deliberations on a forthcoming discussion paper on transfers of a business or entity under common control ('the BCUCC project').

Background

2 In 2012, the BCUCC project was added to the IASB research agenda and in 2014 the IASB made a tentative decision that the scope of the project should consider:

(a) business combinations under common control that are currently excluded from the scope of IFRS 3 *Business Combinations*;

(b) group restructurings; and

(c) the need to clarify the description of business combinations under common control, including the meaning of 'common control'.

3 In October 2017, the IASB clarified that the scope of the BCUCC project would include transactions under common control in which a reporting entity obtains control of one or more businesses, regardless of whether IFRS 3 would identify the reporting entity as the acquirer if IFRS 3 were applied to the transaction.

4 In December 2017, the discussion on the scope was finalised and to also include transactions involving transfers of one or more businesses where all of the combining parties are ultimately controlled by the same controlling party or parties, and the transactions are:

(a) preceded by an external acquisition and/or followed by an external sale of one or more of the combining parties; or

(b) conditional on a future sale such as in an IPO.

Summary of EFRAG TEG and EFRAG CFSS discussion on the scope

5 In November 2017, EFRAG TEG and EFRAG CFSS considered the scope of the project on BCUCC together with the starting point for research and the factors to be considered when deciding on an accounting method for transactions within the scope.

6 EFRAG TEG and EFRAG CFSS were generally supportive of the IASB's proposed scope as it would address transfers of businesses and entities under common control not covered by current guidance, rather than being limited solely to business combinations under common control as defined in IFRS 3.

7 However, EFRAG TEG and EFRAG CFSS did not conclude on whether the acquisition method or the predecessor method was a better starting point to account for business combinations under common control. In their view, selecting a method would depend on the characteristics of the particular transaction.

Current developments on BCUCC project

8 In February 2018, the IASB discussed the starting point in developing proposals for transactions within the scope of the project. In particular, the IASB considered three alternative approaches:

(a) Approach 1 – start from a blank sheet of paper;

(b) Approach 2 – start from IFRS Standards; and

(c) Approach 3 – start from existing practice.

9 Under Approach 1, the *Conceptual Framework for Financial Reporting (Conceptual Framework)* would be used as a guidance to develop an accounting method which would result in useful information about transactions within the scope of the project where the cost is justified by the benefits of the information.

10 Under Approach 2, the starting point would be the existing requirements in IFRS Standards for transactions that are similar to transactions within the scope of the BCUCC project. The IFRS Standards that provide the most appropriate starting point under this approach are:

(a) IFRS 3 for transfer of one or more businesses - IFRS 3 requires the acquirer to account for business combinations applying the acquisition method under which the acquirer recognises the identifiable assets acquired and the liabilities assumed at their acquisition-date fair values and recognises any goodwill or gain from a bargain purchase.

(b) Paragraph 2(b) of IFRS 3 for transfer of a group of items - the Standard requires the acquirer to allocate the cost of the group of items to the individual identifiable assets acquired and liabilities assumed on the basis of their relative fair value at the acquisition date. No goodwill or gain from a bargain purchase is recognised.

(c) IFRS Standards for transfer of a single item - IFRS Standards require the acquirer to recognise acquired items at cost or at fair value depending on the nature of the item.

11 Under Approach 3, the starting point would be the existing practice. BCUCC in practice are most often accounted for applying different variations of the so-called ‘predecessor method’. Under that method, the assets acquired and the liabilities assumed are recognised at their carrying amounts. In certain circumstances, the acquisition method as set out in IFRS 3 is used, however, there is no clear pattern in the application of the two methods.

IASB staff analysis and recommendation

12 The IASB staff proposed that the acquisition method in IFRS 3 is the best starting point in developing proposals for transactions within the scope of the project. The IASB staff recommended taking this approach for the following reason:

(a) the acquisition method is already required for business combinations within the scope of IFRS 3 and hence provides primary users with useful information about such transactions;

(b) the acquisition method is described in IFRS 3 and is tested and well understood;

(c) in some cases is already used in practice to account for BCUCC transactions.

13 Furthermore, using the acquisition method as the starting point means that this method would be applied to those transactions within the scope of the project which are similar enough to a business combination that the same information should be provided. In all the other cases, a different method or methods should be applied to transactions within the scope in order to provide useful information where the cost is justified by the benefits of the information.

IASB tentative decision

14 At its meeting in February 2018, the IASB tentatively decided to use the acquisition method set out in IFRS 3 *Business Combinations* as the starting point in its analysis of transactions within the scope of the project. This, however, will not determine whether the IASB will ultimately propose applying the acquisition method even to a subset of transactions within the scope of the project.

EFRAG's approach

15 The EFRAG Secretariat notes that in trying to help EFRAG TEG forming a view on how to account for the transfer of a business or entity under common control, it has not (initially) asked EFRAG TEG to form a view on which method should be the starting point for accounting for such transfers. Instead, the EFRAG Secretariat suggests that EFRAG TEG first discusses the advantages and disadvantages of each of the methods. Different methods may provide the most useful information under different circumstances and depending on what the objective of the information is (e.g. whether the objective is to estimate future cash flows or assess the management's stewardship). EFRAG TEG members may have divergent views on which method is most useful under given circumstances. The EFRAG Secretariat considers that it would be useful for EFRAG TEG to understand whether divergent views result from:

(a) Disagreements about the advantages and disadvantages of each of the methods; or

(b) Disagreements about what advantages and disadvantages that are most important to consider in specific circumstances.

16 Accordingly, if EFRAG TEG members can generally agree on the advantages and disadvantages of each of the methods, EFRAG TEG can subsequently discuss which advantages and disadvantages are most important in given circumstances.

17 The fact that the EFRAG Secretariat suggests a slightly different approach to consider the issue than the approach followed by the IASB would not necessarily mean that the outcomes would be different.