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Reference to the Conceptual Framework Cover Note

Objective

- 1 The objectives of the session are to:
 - (a) consider the feedback received in response to EFRAG's draft comment letter on the ED/2019/3, *Reference to the Conceptual Framework (Proposed amendments to IFRS 3)*, issued by the IASB on 30 May (the 'ED');
 - (b) discuss and recommend to the EFRAG Board a final comment letter on the ED; and
 - (c) discuss and approve a feedback statement.

Background

- 2 IFRS 3 *Business Combinations* states in paragraph 11:

To qualify for recognition as part of applying the acquisition method, the identifiable assets acquired and liabilities assumed must meet the definitions of assets and liabilities in the Framework for the Preparation and Presentation of Financial Statements at the acquisition date.
- 3 When issuing the revised *Conceptual Framework for Financial Reporting* in March 2018 (the '2018 Conceptual Framework'), the IASB updated many of the references to the Conceptual Framework in IFRS Standards to the revised Conceptual Framework. However, the reference to *Framework for Preparation and Presentation of Financial Statements* in paragraph 11 of IFRS 3 was not updated as the IASB was concerned this could result in unintended consequences.
- 4 In previous versions of the Conceptual Framework, a liability was defined as "a present obligation of the entity arising from past events, the settlement of which is expected to result in an outflow from the entity of resources embodying economic benefits". The 2018 Conceptual Framework defines a liability as "a present obligation of the entity to transfer an economic resource as a result of past events". In the supporting guidance it is mentioned that an obligation is a duty or responsibility that an entity has no practical ability to avoid.
- 5 The definition of a liability in the 2018 Conceptual Framework would in some cases result in levies being recognised earlier than under IFRIC 21 *Levies*. Under IFRIC 21, a liability should not be recognised for a levy that would be calculated by reference to its past activities if the obligation to pay remains conditional on a future activity – even if the entity has no practical ability to avoid that future activity. These requirements are thus not consistent with the guidance included in the 2018 Conceptual Framework. Accordingly, if paragraph 11 of IFRS 3 is amended to refer to the 2018 Conceptual Framework, an entity might have to recognise a liability in

relation to a levy in a business combination but would have to derecognise this on day 2 (resulting in an unintended day 2 gain) as the levy cannot be recognised according to IFRIC 21 which should be used when subsequently accounting for the levy. As IFRIC 21 is an interpretation of IAS 37 *Provisions, Contingent Liabilities and Contingent Assets*, this issue could also arise for other obligations within the scope of IAS 37 that are conditional on an entity's future actions.

- 6 To resolve this issue, the IASB proposed in the ED to:
 - (a) Update the reference in IFRS 3 so that it refers to the 2018 Conceptual Framework.
 - (b) Specify in IFRS 3 that levies within the scope of IFRIC 21 and other obligations within the scope of IAS 37 should be recognised on the acquisition of a business only if they would be identified as present obligations by an entity applying IFRIC 21 or IAS 37.
- 7 In addition, the IASB has tentatively decided to clarify that, in applying the IFRS 3 recognition principle, an acquirer does not recognise contingent assets. Currently, this only appears explicitly in paragraph BC276 of the Basis for Conclusions accompanying IFRS 3.
- 8 The ED proposes that an entity shall apply the amendments to business combinations for which the acquisition date is on or after the beginning of the first annual reporting period beginning on or after the effective date. Earlier application is permitted if at the same time or earlier an entity also applies all the amendments made by *Amendments to References to the Conceptual Framework in IFRS Standards*, issued in March 2018.

EFRAG's initial position on the ED

- 9 In its draft comment letter, EFRAG agreed with the proposals included in the ED.

Comment letters received

- 10 EFRAG published its draft comment letter on 28 June 2019. It received five comment letters from national standard setters and professional organisations.

EFRAG Secretariat recommendation

- 11 Considering the input received from constituents, the EFRAG Secretariat proposes to agree with the ED, that is leaving the draft comment letter unchanged.

Agenda Papers

- 12 In addition to this cover note, agenda papers for this session are:
 - (a) Agenda paper 07-02 – the summary of comments received;
 - (b) Agenda paper 07-03 – the suggested (final) comment letter; and
 - (c) Agenda paper 07-04 – the suggested feedback statement.
- 13 The five comment letters received are available [here](#) under 'Exposure draft consultation'.