

This paper provides the technical advice from EFRAG TEG to the EFRAG Board, following EFRAG TEG's public discussion. The paper does not represent the official views of EFRAG or any individual member of the EFRAG Board. This paper is made available to enable the public to follow the EFRAG's due process. Tentative decisions are reported in EFRAG Update. EFRAG positions as approved by the EFRAG Board are published as comment letters, discussion or position papers or in any other form considered appropriate in the circumstances.

## **Business Combinations under Common Control Cover Note**

### **Objective**

- 1 The purpose of the session is to discuss and approve EFRAG's draft comment letter (the DCL) on the IASB discussion paper DP/2020/2 *Business Combinations under Common Control* (DP).

### **Background**

- 2 The IASB undertook this project to address the lack of guidance in IFRS Standards on how to account for business combinations under common control (BCUCC). At present, entities must apply the requirements included in IAS 8 *Accounting Policies, Changes in Accounting Estimates and Errors* to develop their own accounting policies on the topic. This has resulted in diversity in practice leading to a lack of comparability across entities.
- 3 The objective of the DP is to fill in the gap in financial reporting for BCUCC and explore possible reporting requirements to reduce diversity in practice, improve transparency and provide users with more relevant and comparable information about BCUCC transactions.
- 4 The proposals in the DP are developed from the perspective of the reporting entity (the receiving company) which obtains control of the transferred business. In general, the project is addressing how to report BCUCC in the receiving company's consolidated financial statements. However, for BCUCC which transfer unincorporated business, the proposed requirements would also apply to the separate or individual financial statements of the receiving company.
- 5 In November 2020, the IASB published the [DP](#) with a comment period of 270 days and a comment deadline on 1 September 2021.

### **Summary of preliminary positions included in the EFRAG DCL**

- 6 EFRAG TEG discussed the EFRAG DCL at its meeting on 13 January 2021. The preliminary position taken on the IASB proposals on the project are included below:

#### *Section 1: Scope*

- 7 EFRAG agrees with the scope as proposed by the IASB in its DP. EFRAG welcomes that both BCUCC and group restructurings are considered in the scope.
- 8 However, EFRAG considers that the IASB should align the terminology used in this project with the defined terms in IFRS 3 *Business Combinations*. In particular, the IASB should avoid identifying and labelling group restructurings as a BCUCC especially when such arrangements do not meet the description of a business combination in IFRS 3.

- 9 EFRAG also considers that other common control transactions (e.g., transfer of a group of assets that does not meet the definition of a business) are important and comprehensive topics that need to be discussed in the future.

*Section 2: Selecting the measurement method*

- 10 EFRAG agrees with the IASB that a single measurement approach is not appropriate for all BCUCC.
- 11 EFRAG supports the application of the acquisition method to BCUCC that affect the non-controlling shareholders of the receiving company, subject to the cost-benefit and other practical considerations. EFRAG considers that applying a book-value method to all other BCUCC where ownership interest of the controlling party is unchanged would produce more relevant information about the transaction at lower costs.
- 12 EFRAG is of the view that establishing an appropriate dividing line between applying the acquisition method and a book-value method to BCUCC is very important for achieving the project's objectives. Therefore, EFRAG proposes some modifications to the IASB's decision tree of when to apply each measurement method to BCUCC. In its DCL, EFRAG consults constituents on possible options in order to determine the optimal way to set a dividing line between the two measurement methods suggested in the DP.
- 13 EFRAG supports the optional exemption from the acquisition method for privately-held receiving entities based on a cost-benefit trade-off. However, EFRAG questions whether cost-benefit basis can justify selecting a measurement method based on a decision taken by the non-controlling shareholders of the receiving entity.
- 14 EFRAG also supports the related-party exception to the acquisition method for BCUCC affecting the non-controlling shareholders of a privately-held receiving entity. However, EFRAG is consulting its constituents on whether the related-party exception should be optional rather than mandatory.
- 15 Furthermore, EFRAG agrees with the IASB that the optional exemption and the related-party exception to the acquisition method should not be extended to publicly traded receiving companies. EFRAG is of the view that extending the exemption and the exception to publicly traded receiving companies would be difficult to operationalise or could have limited application in practice.

*Section 3: Applying the acquisition method*

- 16 EFRAG generally agrees with the application of the acquisition method to BCUCC when there are non-controlling shareholders in the receiving entity. In particular, EFRAG agrees that the IASB should not develop a requirement for the receiving company to identify, measure and recognise a distribution from equity but rather recognise any difference between the fair value of consideration paid and the fair value of the identifiable net assets acquired entirely as goodwill.
- 17 Furthermore, the IASB is proposing that the receiving entity should recognise a contribution to equity when the fair value of the consideration paid is lower than in an arm's length transaction. In its DCL, EFRAG does not have a definitive position on this proposal and is consulting constituents on two possible alternatives:
- (a) Alternative 1: Agreeing with the IASB proposals in the DP; and
  - (b) Alternative 2: Proposing the approach consistent with IFRS 3 - recognition of a distribution from equity in goodwill and recognition of a contribution to equity as a gain in profit or loss.

*Section 4: Applying a book-value method*

- 18 In general, EFRAG agrees with the IASB proposals on how to apply a book-value method to BCUCC.
- 19 However, EFRAG is consulting constituents on whether the receiving company should measure the assets and liabilities acquired from the transferred company – either by applying the carrying amounts in the transferred company’s financial statements or use the carrying amounts included in the consolidated financial statements of the transferred company’s controlling party.

*Section 5: Disclosure requirements*

- 20 EFRAG TEG broadly agrees with the proposed disclosure requirements for BCUCC under both the acquisition and a book-value method subject to some drafting changes which could result from the feedback received from constituents on Section 3 of the DCL.

*EFRAG TEG advice to the EFRAG Board*

- 21 EFRAG TEG advises the EFRAG Board to approve the draft comment letter that includes different options and alternatives described above to be consulted on with constituents. Therefore, EFRAG TEG recommends the EFRAG Board to approve the DCL.

**EFRAG TEG voting on the draft comment letter**

- 22 All 13 EFRAG TEG members present at the meeting voted in favour to recommend the DCL to the EFRAG Board, subject to some drafting changes. One EFRAG TEG member was absent from the meeting.

**EFRAG’s comment period timeline**

- 23 The EFRAG Secretariat proposes that the comment period for the EFRAG DCL ends on 30 July 2021. This means that EFRAG TEG would discuss EFRAG’s final comment letter in August 2021 and the EFRAG Board would approve it at its meeting on 7 September 2021.
- 24 The more detailed project planning is included below:

<i>Date</i>	<i>Meeting</i>	<i>Topic</i>
3 February 2021	EFRAG Board	Approve EFRAG’s DCL
30 July 2021		Proposal for EFRAG comment period deadline
August 2021	EFRAG TEG	Discuss and recommend EFRAG’s FCL <sup>1</sup> on the DP
1 September 2021		IASB comment period deadline
7 September 2021	EFRAG Board	Approve EFRAG’s FCL

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<sup>1</sup> Final Comment Letter

**Questions for EFRAG Board**

- 25 Does the EFRAG Board approve EFRAG's draft comment letter recommended by EFRAG TEG?
- 26 Does the EFRAG Board agree with the proposed timeline for the project as included in paragraph 23?

**Agenda Papers**

- 27 In addition to this cover note, agenda papers for this session are:
  - (a) Agenda paper 06-02 – EFRAG draft comment letter on BCUCC; and
  - (b) Agenda paper 06-03 – The IASB Snapshot on BCUCC – for background only.