
Accounting Standards Advisory Forum meeting

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Project	Business Combinations under Common Control
Topic	Initial views—The principle
Contacts	Zicheng Wang (zwang@ifrs.org) Richard Brown (rbrown@ifrs.org)

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Accounting Standards Advisory Forum, December 2022, Agenda paper 4B

This paper will be discussed at the International Accounting Standards Board's (IASB's) November 2022 meeting as Agenda Paper 23B. Agenda papers referred to in this paper are other agenda papers for the IASB's November 2022 meeting, unless otherwise noted.

Introduction and purpose

1. As explained in Agenda Paper 23A, this paper explains our initial views on the principle of selecting the measurement method to apply to business combinations under common control (BCUCCs). This paper does not ask the International Accounting Standards Board (IASB) for decisions.

Structure of this paper

2. The paper is structured as follows:
 - (a) introduction (paragraphs 3–5);
 - (b) analysis of the different approaches (paragraphs 6–28);
 - (c) staff initial views (paragraphs 29–32); and
 - (d) question for the IASB.

Introduction

3. The IASB's preliminary views were that:
 - (a) neither the acquisition method nor a book-value method should apply to all BCUCCs.

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- (b) in principle, the acquisition method should apply to BCUCCs that affect non-controlling shareholders of the receiving entity (NCS)—there was an exemption from, and an exception to, this principle which Agenda Paper 23C [ASAF Agenda Paper 4C] analyses separately; and
 - (c) a book-value method should apply to BCUCCs that do not affect NCS.
4. This paper analyses feedback on the preliminary views as well as respondents' suggestions for other approaches to identify the principle of which measurement method to apply to a BCUCC. The approaches discussed in this paper include:
- (a) applying a book-value method to all BCUCCs (paragraphs 6–11);
 - (b) the preliminary view—considering the effect on NCS (paragraphs 12–19);
 - (c) assessing the substance of each BCUCC (paragraphs 20–24); and
 - (d) allowing an accounting policy choice (paragraphs 25–28).¹
5. Our analysis in this paper builds on our analysis and initial views in Agenda Papers 23D–23H. For each approach we set out the IASB's observations/conclusions in the Discussion Paper *Business Combinations under Common Control* (Discussion Paper) and our analysis of that approach. Paragraphs 29–31 set out our initial views on the principle of which measurement method to apply to a BCUCC after considering our analysis of each possible approach.

Analysis of the different approaches

Applying a book-value method to all BCUCCs

Observations/conclusions in the Discussion Paper

6. Feedback from some stakeholders in developing the Discussion Paper suggested the IASB should require entities to apply a book-value method to all BCUCCs (see paragraphs 2.7–2.9 of the Discussion Paper). These stakeholders said this would, compared to the IASB's preliminary views:
- (a) better improve comparability;
 - (b) provide fewer structuring opportunities; and
 - (c) be less costly.
7. The IASB disagreed because:

¹ A few respondents suggested other approaches for selecting the measurement method which are not included in this agenda paper. We disagreed with those suggestions for reasons explained in other agenda papers including Agenda Paper 23H.

- (a) BCUCCs that affect NCS are similar to business combinations covered by IFRS 3 *Business Combinations* (IFRS 3 BCs)—paragraph 2.20 of the Discussion Paper; and
- (b) for BCUCCs that affect NCS, the composition and common information needs of users are similar to the composition and common information needs of users in an IFRS 3 BC—paragraph 2.22 of the Discussion Paper.

Feedback

8. Most respondents agreed with the preliminary view that neither the acquisition method nor a book-value method should apply to all BCUCCs. Some respondents disagreed with the preliminary view and said a book-value method should apply to all BCUCCs. Paragraphs 16–25 of [Agenda Paper 23B](#) of the IASB's December 2021 meeting provide detailed feedback.

Analysis

9. As Agenda Paper 23F explains, we expect a book-value method to be, on average, less costly to apply than the acquisition method, so this approach would impose the least cost to apply overall. However, we think for some BCUCCs (specifically, BCUCCs that affect NCS):
- (a) a book-value method would not meet common user information needs; and
 - (b) applying the acquisition method would generally meet the cost-benefit trade-off better than applying a book-value method.
10. Applying a book-value method to all BCUCCs would remove opportunities to structure a BCUCC to qualify for either the acquisition method or a book-value method. However, as Agenda Paper 23G explains, some structuring opportunities could still exist:
- (a) to structure an IFRS 3 transaction to be under common control (so a book-value method would apply) or not under common control (so the acquisition method would apply)—see paragraph 11 of Agenda Paper 23G; or
 - (b) when applying a book-value method—see paragraphs 30–32 of Agenda Paper 23G.
11. As Agenda Paper 23D explains, we think the nature of all BCUCCs is similar to IFRS 3 BCs. While applying a book-value method to all BCUCCs would improve comparability between BCUCCs, it would not result in comparable information for BCUCCs and IFRS 3 BCs (Agenda Paper 23H).

The preliminary view—considering the effect on NCS

Observations/conclusions in the Discussion Paper

12. The IASB's preliminary views were that in principle, the acquisition method should apply to BCUCCs that affect NCS and a book-value method should apply to BCUCCs that do not affect NCS.

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13. As paragraphs 2.20–2.33 of the Discussion Paper explain, in reaching this conclusion the IASB considered that:
- (a) for BCUCCs which affect NCS:
 - (i) the transactions are similar to IFRS 3 BCs; and
 - (ii) users' common information needs are similar to an IFRS 3 BC;
 - (b) for BCUCCs which do not affect NCS:
 - (i) there is no change in the ultimate ownership interest in the transferred business;
 - (ii) similar information would be produced regardless of whether a BCUCC takes place and how the controlling party structures any combination;
 - (iii) applying the acquisition method to a BCUCC involving wholly-owned entities may be difficult and, if consideration paid for a BCUCC differs from consideration that would have been paid to an unrelated party, the receiving entity might measure goodwill at an arbitrary amount that does not provide useful information; and
 - (iv) a book-value method is typically less costly to apply and would provide useful information; and
 - (c) determining the measurement method based on whether NCS are affected is objective so would reduce complexity because entities would not have to develop their own accounting policy.
14. The IASB considered that its preliminary views would meet the project's objective of reducing diversity in practice, improving transparency of reporting and providing better information about BCUCCs while taking appropriate account of the cost–benefit trade-off. The IASB's preliminary views would reduce diversity in practice by specifying which method should apply in which circumstances (see paragraphs 2.56–2.58 of the Discussion Paper).

Feedback

BCUCCs that affect NCS

15. Paragraphs 26–40 of [Agenda Paper 23B](#) of the IASB's December 2021 meeting provide detailed feedback on the principle of applying the acquisition method to BCUCCs that affect NCS. In summary:
- (a) many respondents agreed with the preliminary view;

- (b) some respondents generally agreed but suggested modifications—most commonly applying a book-value method to a BCUCC that affects NCS if the NCS are insignificant;² and
- (c) many respondents disagreed, of which:
 - (i) some said a book-value method should apply to all BCUCCs (see paragraphs 6–11);
 - (ii) some said the receiving entity should assess the substance of the BCUCC (see paragraphs 20–24); or
 - (iii) some said the receiving entity should have a policy choice (see paragraphs 25–28).

BCUCCs that do not affect NCS

16. Paragraphs 41–50 of [Agenda Paper 23B](#) of the IASB’s December 2021 meeting provide detailed feedback on applying a book-value method to BCUCCs that do not affect NCS. In summary:
- (a) many respondents agreed with the preliminary view; and
 - (b) many respondents disagreed, of which:
 - (i) most said the acquisition method should apply in specific circumstances (most commonly if the receiving entity has publicly traded debt, which is considered separately in paragraphs 71–79 of [Agenda Paper 23C](#) [ASAF [Agenda Paper 4C](#)]) but otherwise agreed with the preliminary view;
 - (ii) a few said the receiving entity should assess the substance of the BCUCC (see paragraphs 20–24); and
 - (iii) a few said the receiving entity should have a policy choice (see paragraphs 25–28).

Other

17. Respondents requested clarification on various aspects the IASB’s preliminary view, including the meaning of ‘shareholders’ and ‘affects’—these requests are summarised in Appendix A of [Agenda Paper 23C](#) to the IASB’s December 2021 meeting. If the IASB tentatively decides to pursue this principle, we will provide detailed analysis in a future meeting so the IASB can decide whether and how to respond to the clarification requests. We think these requests do not introduce unexpected complexity in applying the IASB’s preliminary view and should not affect a tentative decision on whether to pursue this principle.

² We use the term ‘insignificant’ for simplicity—however, these respondents suggested various thresholds, including for example considering only NCS that are ‘significant’ / ‘material’ / ‘substantive’, disregarding NCS that are ‘insignificant’ / ‘immaterial’ / ‘de minimis’ or disregarding NCS ‘without significant influence’. Some respondents referred to the NCS whilst others referred to the ownership interests held by NCS.

Analysis

18. We think applying the acquisition method to BCUCCs that affect NCS and a book-value method to BCUCCs that do not affect NCS reflects an appropriate balance of the factors considered in different agenda papers. Specifically, in our view:
- (a) this approach meets common user information needs;
 - (b) this approach generally meets the cost-benefit trade-off because:
 - (i) for BCUCCs that affect NCS, the cost-benefit trade-off is comparable to IFRS 3 BCs; and
 - (ii) for BCUCCs that do not affect NCS, either method could meet common user information needs and we expect a book-value method to be less costly;
 - (c) although the accounting for all BCUCCs would not be comparable, this approach:
 - (i) results in comparability between BCUCCs in similar circumstances; and
 - (ii) provides comparability between BCUCCs that affect NCS and IFRS 3 BCs;
 - (d) this approach avoids the acquisition method applying to BCUCCs that do not affect NCS, which we think could create significant practical challenges; and
 - (e) although this approach could create some structuring opportunities to qualify for a particular measurement method (for example, BCUCCs could be structured with insignificant NCS), some such structuring opportunities will exist unless the acquisition method applies to all BCUCCs as well as to IFRS 3 BCs.
19. Agenda Paper 23C [ASAF Agenda Paper 4C] considers exceptions and exemptions to this principle which could, for example, reflect the cost-benefit trade-off for particular BCUCCs or minimise structuring opportunities.

Assessing the substance of each BCUCC

Observations/conclusions in the Discussion Paper

20. In developing its preliminary views, the IASB considered whether entities should evaluate how similar a BCUCC is to an IFRS 3 BC in order to determine which method to apply. As explained in paragraphs 2.18–2.19 of the Discussion Paper, the IASB decided not to base the selection of the measurement method on such an evaluation because:
- (a) it would be difficult to provide a workable set of indicators;
 - (b) applying such indicators would be subjective so may not help reduce diversity in practice; and

- (c) some of the indicators (for example, the purpose of the combination or the process for deciding the terms of the combination) would not affect what information would be most useful to users.

Feedback

- 21. Respondents said the receiving entity should apply either the acquisition method or a book-value method depending on the substance of the BCUCC:
 - (a) to BCUCCs that affect NCS (some respondents); and
 - (b) to BCUCCs that do not affect NCS (a few respondents).
- 22. Paragraphs 34–36 and paragraph 47 of [Agenda Paper 23B](#) of the IASB's December 2021 meeting provide detailed feedback.

Analysis

- 23. Whilst we acknowledge this approach might reduce structuring opportunities compared to the IASB's preliminary views (because an entity would determine the measurement method based on the substance of the BCUCC), we continue to agree with the IASB's reasons for not using this approach in developing its preliminary views. In particular, we think that:
 - (a) it would be difficult to provide a workable set of indicators;
 - (b) applying such indicators would be subjective so may not help reduce diversity in practice; and
 - (c) apart from NCS, the indicators suggested by respondents would not affect what information is most useful to investors.
- 24. Further, as explained in Agenda Paper 23D, our initial view is that the nature of all BCUCCs is similar to IFRS 3 BCs.

Accounting policy choice

Observations/conclusions in the Discussion Paper

- 25. The Discussion Paper did not discuss allowing the receiving entity a choice of applying either the acquisition method or a book-value method to BCUCCs.

Feedback

- 26. Respondents suggested allowing the receiving entity a choice of applying either the acquisition method or a book-value method:
 - (a) to BCUCCs that affect NCS (some respondents); and
 - (b) to BCUCCs that do not affect NCS (a few respondents).

27. Paragraphs 37–39 and paragraph 46 of Agenda Paper 23B of the IASB’s December 2021 meeting provide detailed feedback.

Analysis

28. While this approach would allow the receiving entity to consider whether the benefits to its users justify the costs of applying each method, we think the IASB should not consider this approach further because:
- (a) there would be little comparability between BCUCCs because entities could choose to apply different methods to BCUCCs in similar circumstances—this approach would not reduce diversity in practice, part of the project objective; and
 - (b) we think for some BCUCCs (specifically, BCUCCs that affect NCS) this approach would not meet common user information needs.

Staff initial views

Our initial views

29. We continue to agree with the IASB’s preliminary view that neither the acquisition method nor a book-value method should apply to all BCUCCs. In particular, we disagree with:
- (a) applying a book-value method to all BCUCCs for the reasons explained in paragraphs 9–11; and
 - (b) applying the acquisition method to all BCUCCs—amongst other reasons, we think the costs would outweigh the benefits for some BCUCCs.
30. We continue to agree with the IASB’s preliminary views to, in principle, apply the acquisition method to BCUCCs that affect NCS and a book-value method to BCUCCs that do not affect NCS for the reasons explained in paragraphs 18–19.
31. On balance, we think this approach provides the most useful information whilst considering the cost-benefit trade-off, structuring opportunities and other considerations. We acknowledge there are disadvantages to this approach, specifically:
- (a) it would not result in comparability between all BCUCCs—although it would result in comparability between BCUCCs in similar circumstances; and
 - (b) it could create some structuring opportunities to structure BCUCCs with insignificant NCS—although, as paragraph 32 explains, Agenda Paper 23C [ASAF Agenda Paper 4C] considers exceptions and exemptions which could help minimise such structuring opportunities.

Exceptions to the principle

32. Although we think applying the acquisition method to BCUCCs that affect NCS and a book-value method to BCUCCs that do not affect NCS is an appropriate principle, Agenda Paper 23C [ASAF Agenda Paper 4C] considers whether, due to cost-benefit or other considerations such as to minimise structuring opportunities, a different method should apply in particular situations. Specifically, Agenda Paper 23C [ASAF Agenda Paper 4C] considers whether:

- (a) to apply a book-value method to some BCUCCs that affect NCS; and
- (b) to apply the acquisition method to some BCUCCs that do not affect NCS.

Questions for the IASB

Do IASB members have comments or questions on the analysis in this paper? Specifically:

- (a) is there any analysis that is unclear, including analysis in the relevant supporting papers (Agenda Papers 23D–23H)?
- (b) is there anything IASB members would like us to research or analyse further before the IASB makes tentative decisions on selecting the measurement method to apply to BCUCCs?
- (c) do IASB members have any other comments or questions on the analysis in this paper or the staff initial views summarised in paragraphs 29–31?