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EFRAG – European Financial Reporting Advisory Group
35 Square de Meeûs
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Att.: Ms Ioana Kiss

By e-mail: ioana.kiss@efrag.org

23 June 2021

Dear Ms Ioana Kiss,

EFRAG's Draft Comment Letter on the IASB's Discussion Paper DP/2020/2 *Business Combinations under Common Control*

The Danish Accounting Standards Committee ('DASC') set up by FSR – Danish Auditors ('FSR' or 'FSR – danske revisorer') is pleased to respond to EFRAG's Draft Comment Letter (the 'DCL') on the IASB's Discussion Paper DP/2020/2 *Business Combinations under Common Control* (the 'DP' or 'BCUCC')*.*

Our response is included in the appendix to this letter. Please note that it has been necessary for DASC to prioritise the questions selecting those we consider the most important.

We would like to emphasise that the above-mentioned decision is not in any way meant to suggest that the questions we have omitted are not relevant.

If you have any questions or comments, please do not hesitate to contact us.

Kind regards,

Torben Johansen
DASC Chairman

Jan Peter Larsen
DASC International Relations

Appendix

Question 1
Paragraphs 1.10–1.23 discuss the IASB's preliminary view that it should develop proposals that cover reporting by the receiving company for all transfers of a business under common control (in the Discussion Paper, collectively called business combinations under common control) even if the transfer:

(a) is preceded by an acquisition from an external party or followed by a sale of one or more of the combining companies to an external party (that is, a party outside the group); or

(b) is conditional on a sale of the combining companies to an external party, such as in an initial public offering.

DASC comments
DASC agrees with EFRAG.

In our jurisdiction most - if not all - BCUCC transactions comprise internal group restructurings. Therefore, from a Danish perspective the most prevalent issue is how to account for such internal group BCUCC in the separate financial statements. Therefore, we see a link from this project into the project on application of the equity method.

Question to Constituents [18-19]
18 Some stakeholders have raised questions about the meaning of 'transitory control', for example, in submissions to the IFRS Interpretations Committee. The IASB avoids the discussion on transitory control by including in the scope all transfers of business under common control.

19 Do you consider that it is important to clarify the meaning of "transitory control" for BCUCC, even if in the DP, the IASB addresses the issue by including in the scope all transfers of business under common control?

DASC comments [18-19]
For some jurisdiction's, clarification of "transitory control" may be important. Given our response to Question 1 we have not experienced significant discussions of transitory control in Denmark.

Question to Constituents [29]
29 Do you consider that the definition of BCUCC as described in the DP:

(a) results in transactions being included in the scope of the project that should not be within the scope; and

(b) are there transactions outside the scope of the project that should be within the scope?

DASC comments [29]
Generally, DASC has no problem with the scope proposed in the ED. That said, we are mindful of point 26 in EFRAG's DCL that it may give rise to consideration in the future about possible modifications to IFRS Standards. We refer to our response to Question 1 re. issues for the separate financial statements and the link to the project re. the equity method.

In our view, the importance of the BCUCC project is to keep its focus on those transactions currently being scoped out of IFRS 3.

Question 2
Paragraphs 2.15–2.34 of the DP discuss the IASB's preliminary views that:

(a) neither the acquisition method nor a book-value method should be applied to all business combinations under common control.

Do you agree? Why or why not? If you disagree, which method do you think should be applied to all such combinations and why?

(b) in principle, the acquisition method should be applied if the business combination under common control affects non-controlling shareholders of the receiving company, subject to the cost–benefit trade-off and other practical considerations discussed in paragraphs 2.35–2.47 of the DP.

Do you agree? Why or why not? If you disagree, in your view, when should the acquisition method be applied and why?

(c) a book-value method should be applied to all other business combinations under common control, including all combinations between wholly-owned companies.

Do you agree? Why or why not? If you disagree, in your view, when should a book-value method be applied and why?

DASC comments
We agree with EFRAG.

Although the IASB's proposal is not without problems, we do not see a better alternative when agreeing that there can hardly be one method that fits all. The big question here is to determine where to draw the line between one method over the other. Without a proposal from the IASB, the world of accounting for BCUCC would remain unchanged.

The DP mentions whether the business combination under common control affects non-controlling shareholders of the receiving company. DASC discussed whether it would also be relevant to include loan providers, for instance those holding a company's listed bonds and other providers of credit. In addition, loan providers of a loan to an entity that is close to breaking its covenants may also have an interest. That said, we are mindful that it will be difficult to determine how broad this should be.

Questions to Constituents [49-50]
49 Do you agree that a single measurement approach is not appropriate for all BCUCC? Based on the pros and cons of applying the acquisition method (described in paragraph 37) and a book-value method (described in paragraph 38), do constituents support these two methods being applied to particular subset of BCUCC?

50 In your jurisdiction, are there any requirements on how to account for BCUCC?

(a) If so, describe the requirements;

(b) If not, what is the current practice in your jurisdiction?

(c) For (a) and (b) above, where is the difference between the consideration paid by the receiving company and the acquired net assets recognised when:

(i) the consideration paid is higher than the acquired net assets; and

(ii) the consideration paid is lower than the acquired net assets?

DASC comments [49-50]
Referring to our response to Question 2 DASC agrees that a single measurement approach is not appropriate for all BCUCC.

The Danish Financial Statements Act ('DFSA') is in the field of business combinations interpreted by the guidance in IFRS 3 once the business combination has a certain complexity. Prior to IFRS 3, the DFSA was interpreted by the guidance in IAS 22. There are provisions in the DFSA when two enterprises are both subject to a parent in a group or are both subject to the control of the same interest. The provision reads, in part:

... Where, in connection with the establishment of the group, the two enterprises are both subject to a parent in a group or are both subject to the control of the same interest, the group establishment may be treated in accordance with the uniting of interests method.

And another provision describes briefly the uniting of interests method:

Under the uniting of interests method, the consolidated financial statements are presented for the period in which the interests are united as if the enterprises had been combined starting from the earliest accounting period covered by the financial statements.

(2) However, the enterprise may decide to consider the uniting of interests as having taken place at the acquisition date.

(3) The difference between the amount paid as contributed capital and any share premium plus any cash consideration and the equity value of the subsidiary must in a clear manner be added to or deducted from the reserves available for the covering of loss.

Thus, the DFSA allows for use of the uniting of interests method as well as the book value method in the situations referred to above.

As mentioned in our response to Question 1, most – if not all – BCUCC in our jurisdiction comprise internal group restructurings.

Question 3
DASC did not discuss this question.

Questions to Constituents [65-66]
65 Do you agree with EFRAG's suggestion in paragraph 62 to reverse the order of Step 1 and Step 2 of the decision tree when selecting the measurement method for BCUCC?

66 Considering the options provided in paragraph 64 on how to modify the scope of the IASB's decision tree for selecting the measurement method for BCUCC, which option do you prefer? Please explain what your main considerations are for selecting that particular option.

DASC comments [65-66]
As mentioned in our response to Question 1, most – if not all – BCUCC in our jurisdiction comprise internal group restructurings. Therefore, we do not state any preference for the options in para 64. In the discussion around the decision tree, we agree with the EFRAG proposal.

Question to Constituents [69]
69 Considering the proposed options to modify the IASB's decision tree as explained in paragraphs 62 and 64, do you consider that applying the optional exemption from the acquisition method, in particular, requesting approval from non-controlling shareholders would raise any concerns? Please explain.

DASC comments [69]
One concern may be that some of the NCI's do not get the information of the fair values they may need to continue accounting for their share of the combined entity when the acquisition method is not applied to a transaction.

Question to Constituents [72]
Considering the arguments in paragraph 71, do you agree that the related-party exception provided by the IASB should be rather 'permitted' under the proposals and not 'required'? If you disagree, please explain.

DASC comments [72]
We agree with EFRAG that the related-party exception provided by the IASB should be 'permitted' rather than 'required'.

Question 4
Paragraphs 2.48–2.54 of the DP discuss suggestions from some stakeholders that the optional exemption from and the related-party exception to the acquisition method should also apply to publicly traded companies. However, in the IASB's preliminary view, publicly traded receiving companies should always apply the acquisition method.

(a) Do you agree that the optional exemption from the acquisition method should not be available for publicly traded receiving companies? Why or why not? If you disagree, in your view, how should such an exemption be designed so that it is workable in practice?

(b) Do you agree that the related-party exception to the acquisition method should not apply to publicly traded receiving companies? Why or why not?

DASC comments
DASC agrees with EFRAG.

As mentioned in our response to Question 2, the big question is to determine where to draw the line. It may be difficult - if not impossible - to reach all NCI's. In addition, not extending to publicly traded companies will have the advantage of not complicating the proposal unnecessarily.

Question 5
Paragraphs 3.11–3.20 discuss how to apply the acquisition method to business combinations under common control.

(a) In the IASB's preliminary view, it should not develop a requirement for the receiving company to identify, measure and recognise a distribution from equity when applying the acquisition method to a business combination under common control.

Do you agree? Why or why not? If you disagree, what approach for identifying and measuring a distribution from equity do you recommend and why? In particular, do you recommend either of the two approaches discussed in Appendix C or do you have a different recommendation?

(b) In the IASB's preliminary view, it should develop a requirement for the receiving company to recognise any excess fair value of the identifiable acquired assets and liabilities over the consideration paid as a contribution to equity, not as a bargain purchase gain in the statement of profit or loss, when applying the acquisition method to a business combination under common control.

Do you agree? Why or why not? If you disagree, what approach do you recommend and why?

(c) Do you recommend that the IASB develop any other special requirements for the receiving company on how to apply the acquisition method to business combinations under common control? If so, what requirements should be developed and why are any such requirements needed?

DASC comments
DASC agrees with EFRAG.

We agree that the IASB should not develop requirements because it would have widespread consequences on common control transactions in general determining whether they are concluded on arm's length basis or not.

We agree that adjustment, whether being positive or negative, should be accounted for within equity. In addition, local company law may impose different treatments depending on whether the transaction is considered a distribution from or a contribution to equity. Therefore, we do not believe that the IASB should develop any requirements in this area.

Questions to Constituents [99-100]
99 Which of the two alternatives do you consider will provide the most useful information? Please explain.

100 If neither, which other approach do you recommend and why?

DASC comments [99-100]
As EFRAG, DASC also has consistency with IFRS 3 as a high priority when applying the acquisition method to BCUCCs. Hence, our preference is for alternative 2.

Question 6
Paragraphs 4.10–4.19 discuss the IASB's preliminary view that, when applying a book-value method to a business combination under common control, the receiving company should measure the assets and liabilities received using the transferred company's book values.

Do you agree with the IASB's preliminary view? Why or why not? If you disagree, what approach do you suggest and why?

DASC comments
DASC agrees as such with EFRAG. To keep it simple, DASC prefers using the book values recorded in the consolidated financial statements of the transferred company's controlling party in order not to lose these numbers in a subsequent BCUCC.

Based on our experience the approach applied in our jurisdiction both encompasses the transferred entity's book values and the controlling party's book values. Both approaches are accepted under local GAAP (DFSA).

Questions to Constituents [107-109]

107 EFRAG acknowledges that in some jurisdictions, the local regulator may dictate that a particular method be used. What approach is currently being applied in the financial statements in your jurisdiction? Please provide a description of this approach.

108 Do you agree with using the transferred entity's book values or with using the controlling party's book values? Please explain your reasons why.

109 If you do not agree with either approach, what approach do you suggest and why?

DASC comments [107-109]

Please see our response Question 6.

Question 7

Paragraphs 4.20–4.43 discuss the IASB's preliminary views that:

(a) the IASB should not prescribe how the receiving company should measure the consideration paid in its own shares when applying a book-value method to a business combination under common control; and

(b) when applying that method, the receiving company should measure the consideration paid as follows:

(i) consideration paid in assets—at the receiving company's book values of those assets at the combination date; and

(ii) consideration paid by incurring or assuming liabilities—at the amount determined on initial recognition of the liability at the combination date applying IFRS Standards.

DASC comments

DASC agrees with EFRAG that the IASB proposal should not prescribe how the receiving company should measure the consideration paid in its own shares. In this area, there may also be local requirements in company law that will take precedence. For instance, Danish company law requires a transaction like the one mentioned in (b)(i) be accounted at fair value.

DASC favors symmetry. If liabilities are required to be measured at fair value by the reference to IFRS Standards, DASC considers the same measurement attribute should apply to the asset.

Question to Constituents [125]

125 Are there other forms of consideration paid apart from those identified in the DP, e.g., consideration paid in the form of a transfer of an unincorporated business, and how common are these forms of payment?

DASC comments [125]

What comes to our mind is barter transactions. These are very rare in our jurisdiction.

Question 8

Paragraphs 4.44–4.50 discuss the IASB's preliminary views that:

(a) when applying a book-value method to a business combination under common control, the receiving company should recognise within equity any difference between the consideration paid and the book value of the assets and liabilities received; and

(b) the IASB should not prescribe in which component, or components, of equity the receiving company should present that difference.

Do you agree with the IASB's preliminary views? Why or why not? If you disagree, what approach do you suggest and why?

DASC comments
DASC agrees with EFRAG to recognise within equity any difference between the consideration paid and the book value of the assets and liabilities received.

DASC also agrees with EFRAG not specifying in which component(s) of equity the difference between consideration paid and assets and liabilities received should be presented because such specification may conflict with national company law.

That said, DASC considered whether it should be possible to apply the acquisition method when cash or other assets are issued. Otherwise, it may run the risk of wiping out equity even if the transaction is "paying fair value for fair value".

Question 9
DASC did not discuss this question.

Question 10
Paragraphs 4.57–4.65 discuss the IASB's preliminary view that, when applying a book-value method to a business combination under common control, the receiving company should include in its financial statements the assets, liabilities, income and expenses of the transferred company prospectively from the combination date, without restating pre-combination information.

Do you agree with the IASB's preliminary view? Why or why not? If you disagree, what approach do you suggest and why?

DASC comments
As such, DASC understands EFRAG's response. We have under local GAAP the possibility to choose between combination date or the beginning of the reporting period (typically 1 January) if the transaction is driven by company law such as a legal merger. We, therefore, favour a choice rather than a requirement to use the combination date, supplemented by adequate disclosures to explain what has happened.

Question 11
Paragraphs 5.5–5.12 of the DP discuss the IASB's preliminary views that for business combinations under common control to which the acquisition method applies:

(a) the receiving company should be required to comply with the disclosure requirements in IFRS 3 Business Combinations, including any improvements to those requirements resulting from the Discussion Paper Business Combinations - Disclosures, Goodwill and Impairment; and

(b) the IASB should provide application guidance on how to apply those disclosure requirements together with the disclosure requirements in IAS 24 Related Party Disclosures when providing information about these combinations, particularly information about the terms of the combination.

Do you agree with the IASB's preliminary views? Why or why not? If you disagree, what approach do you suggest and why?

DASC comments
DASC supports disclosure requirements for BCUCC accounted for under the acquisition method if these disclosure requirements are not excessive but of course enough to provide relevant information to the users of the financial statements.

Question 12
Paragraphs 5.13–5.28 of the DP discuss the IASB's preliminary views that for business combinations under common control to which a book-value method applies:

(a) some, but not all, of the disclosure requirements in IFRS 3 Business Combinations, including any improvements to those requirements resulting from the Discussion Paper Business Combinations - Disclosures, Goodwill and Impairment, are appropriate (as summarised in paragraphs 5.17 and 5.19) of the DP;

(b) the IASB should not require the disclosure of pre-combination information; and

(c) the receiving company should disclose:

(i) the amount recognised in equity for any difference between the consideration paid and the book value of the assets and liabilities received;

and

(ii) the component, or components, of equity that includes this difference.

Do you agree with the IASB's preliminary views? Why or why not? If you disagree, what approach do you suggest and why?

DASC comments
DASC supports disclosure requirements for BCUCC accounted for under the book-value method if these disclosure requirements are not excessive but of course enough to provide relevant information to the users of the financial statements.