ICAEW
TECHNICAL ADVISORY SERVICE

HIVE UP UNDER FRS 102

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INTRODUCTION

This helpsheet has been issued by ICAEW's Technical Advisory Service to help members understand accounting for a hive up under FRS 102. The term 'hive up' is commonly used to describe a type of reorganisation within a group of companies where the net assets of, and business undertaken by, a subsidiary are transferred up into the parent company.

Members may also wish to refer to the following related helpsheet and guidance:

- Intangible assets and goodwill under FRS 102
- TECH 02/17 BL Guidance on realised and distributable profits under the Companies Act 2006

ACCOUNTING FOR A HIVE UP

The relevant requirements in FRS 102 can be found in Section 19. In particular, paragraphs 19.3 to 19.5 define a business combination and paragraph 19.22 covers the treatment of goodwill. Members may wish to refer to the helpsheet Intangible assets and goodwill under FRS 102 for further considerations in relation to goodwill.

A business combination is defined as the bringing together of separate entities or businesses into one reporting entity.

When a company acquires shares in another company, separate recognition of goodwill in the parent company's own accounts is not usually appropriate. However, where the underlying trade and assets (the business) are then subsequently 'hived up' to the parent, it is reasonable to take the approach required for a business combination under FRS 102. The justification would be that, although the initial investment was in shares, this was represented by the underlying trade and assets which are 'acquired' through the hive up, either at the same time or subsequently. It is also important to ensure that any goodwill recognised is that calculated based on the original acquisition, **not** when the hive up occurs.

The following example illustrates the accounting double entries for a simple hive up scenario. It is worth noting that the example laid out below applies the principles of hybrid accounting – this is an approach that works to apply the principles of merger accounting (a consolidation approach) to the individual accounts of an entity that has acquired the trade and assets of another entity as part of a group reconstruction. This is an optional approach where it applies, an entity could choose to apply the principles of acquisition accounting but generally it is accepted that in most cases undertaking a fair value exercise will not be appropriate.

EXAMPLE

Company P buys the shares of company S for £50,000. The starting positions and effects of the following journals at each step are shown in the table below for both the parent (P) and the subsidiary (S).

	Balance Sheet, at acquisition	
	P	**S**
Net assets	100,000	20,000
Goodwill	0	0
Cost of investment	50,000	0
Intercompany balance	0	0
	150,000	20,000
Share capital	60,000	10,000
Reserves	90,000	10,000
	150,000	20,000

Step 1

Transfer net assets up at book value.

P's books

Dr net assets	20,000
Cr intercompany balance	20,000

S's books

Dr intercompany balance	20,000
Cr net assets	20,000

	Balance Sheet, step one - assets up	
	P	S
Net assets	120,000	0
Goodwill	0	0
Cost of investment	50,000	0
Intercompany balance	(20,000)	20,000
	150,000	20,000
Share capital	60,000	10,000
Reserves	90,000	10,000
	150,000	20,000

Step 2

Transfer goodwill out of cost of investment (calculated as cost of investment less fair value of tangible net assets acquired [50,000-20,000]). Goodwill is then amortised over the useful economic life. Note: this goodwill calculation is based on the original acquisition of the subsidiary, we are not creating goodwill as part of the application of hybrid accounting.

P's books

Dr goodwill	30,000
Cr cost of investment	30,000

	Balance Sheet, step two - goodwill reclassification	
	P	S
Net assets	120,000	0
Goodwill	30,000	0
Cost of investment	20,000	0
Intercompany balance	(20,000)	20,000
	150,000	20,000
Share capital	60,000	10,000
Reserves	90,000	10,000
	150,000	20,000

Step 3

P will decide the way forward for S at this point, but assuming S is no longer required, the intercompany balance could be reduced by a dividend from S to P.

Other alternatives could include a formal liquidation or a dividend followed by application to strike the company off the register. A reduction in capital could be performed under s641 of the Companies Act 2006 to extract the value of the share capital and avoid the assets reverting to the Crown under the bona vacantia rules when the company is struck off.

Impairment

The hive up of trade and assets and subsequent plans for S would be an indicator of impairment, therefore both the cost of investment and goodwill value in P will need an impairment review to be undertaken.

An asset must be reduced down to its recoverable amount when this is below its carrying amount (FRS 102 27.5).

An assets recoverable amount is the higher of its fair value less costs to sell and value in use. Members may wish to refer to the ICAEW webpage Impairment of assets for guidance available on impairments under FRS 102.

VARIATIONS

There are a number of common variations on a standard hive up procedure, a selection of which are explored below.

Hive up several years after acquisition

Where a hive up is performed several years after acquisition, the goodwill would have to be established based on fair values of net assets at the time of acquisition of the subsidiary, **not** at the point of hive up. However, some or all of that goodwill transferred from the investment on hive up will then need to be written down to reflect the amortisation arising from the date of initial acquisition to the time of the hive up. This is to take account of the fact that part or all of the useful economic life has already elapsed. Therefore, the goodwill recognised at the date of hive up is the amortised amount, with the accumulated amortisation adjusting reserves at the date of the hive up (it is not a prior period error). This treatment is parallel to the amortisation of goodwill in the consolidated accounts where prepared.

Hive across

The same principles discussed above in relation to hive ups could be modified and applied to a ‘hive across’ where a business and the associated assets and liabilities are transferred between two subsidiaries within a group.

It is worth considering the impacts in the parent company because value is moving from one subsidiary to another. Where the transferring subsidiary has not been appropriately recompensed for the trade and assets it is generally accepted that the parent may adjust its cost of investment in the two subsidiaries to reflect the redistribution of value between the two entities – i.e. we will see the value of the transferring subsidiary reduce, and the value of the receiving subsidiary increase by an equal amount. There is no gain or loss in the parent, just a reallocation.

Where trade and assets are transferred between subsidiaries for less than their fair value it is also important to consider whether this constitutes a distribution in legal terms. If a distribution is created, the gifting company will need sufficient distributable reserves for this to be legal.

Hive up of net liabilities

Another variation arises where a subsidiary hives up net liabilities to the parent. Whilst this is not particularly common, one approach to accounting for this could be to follow similar principles.

If the hive up steps are followed as stated above, the parent will end up with a debtor balance and what appears to be a negative cost of investment, while the subsidiary will have a creditor due to the parent. As the trade and assets have been hived out of the subsidiary, realistically the parent isn't going to be able to recover the debt and therefore the parent would usually Dr Cost of investment and Cr Intercompany balance. The subsidiary would still be required to show the liability until the balance is legally waived by the parent, when it would be reclassified to equity as a capital contribution.

OTHER CONSIDERATIONS

The above helpsheet addresses the basic questions arising out of a hive up and is not intended as a comprehensive solution for all group reorganisation exercises.

In addition to the accounting issues explored above, there may also be issues related to tax and distributable profits which should be explored and addressed before the hive up occurs. Members should refer to ICAEW TECH 02/17 BL Guidance on realised and distributable profits under the Companies Act 2006.

IF IN DOUBT SEEK ADVICE

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