ICAEW
REPRESENTATION 82/21

DISCUSSION PAPER DP 2020/2 BUSINESS COMBINATIONS UNDER COMMON CONTROL

Issued 1 September 2021

ICAEW welcomes the opportunity to comment on *Discussion Paper DP 2020/2 Business Combinations under Common Control* published by the IASB in November 2020, a copy of which is available from this link.

The current gap in IFRS standards leads to diversity in practice and needs to be filled. We agree with the Board's conclusion that one size doesn't fit all but feel that its proposed solution is too prescriptive. An alternative approach is highlighted in the 'key points' section below and expanded upon throughout this letter.

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KEY POINTS

FILLING THE GAP

1. The lack of an IFRS standard dealing with the topic of business combinations under common control (BCUCC) means that diversity in practice exists in circumstances where fact patterns are similar. This can make it difficult for investors and other users of the financial statements to understand the effects of these transactions and to compare companies that undertake them. We therefore agree that the current gap in IFRS standards needs to be filled.
2. We note, however, that the project's scope includes group restructurings. Some group restructurings – such as where a business is transferred to a newly incorporated or shell company – will not meet the definition of a business combination and the Board should avoid creating confusion by labelling them as such. We recommend that the project is renamed to make it clear that it encompasses a wider range of transactions.

GROUP RESTRUCTURINGS THAT ARE NOT BUSINESS COMBINATIONS

3. The discussion paper currently includes limited guidance on accounting specifically for group restructurings that do not meet the definition of a business combination. We believe that in many – possibly all – circumstances, a book-value approach should be applicable to such group restructurings, even when there are non-controlling interests in the receiving company.
4. Giving clear direction through application guidance could be a way to simplify the analysis required for these transactions and to address our concerns about potential confusion with transactions that are business combinations. Alternatively, such group restructurings could be spun off into a separate project if keeping them within scope is likely to cause delays to the long-awaited guidance on BCUCC.

ONE SIZE DOESN'T FIT ALL

5. We agree with the Board's conclusion that one size doesn't fit all and that some BCUCC should be accounted for using the acquisition method and that others should be accounted for using a book-value method. The situations in which such business combinations occur are many and various and it is therefore appropriate that differences arise in the accounting used to report them.
6. We agree that the accounting in this area should be driven by user needs. Just as the situations in which BCUCC occur are many and various so too are the needs of users of financial information relating to these transactions. The Board's preliminary views acknowledge these differing needs and accept that the method used should depend on the circumstances.
7. While we are supportive of the Board's attempts to reduce the current diversity in practice, we do not fully support the proposals set out in the discussion paper.

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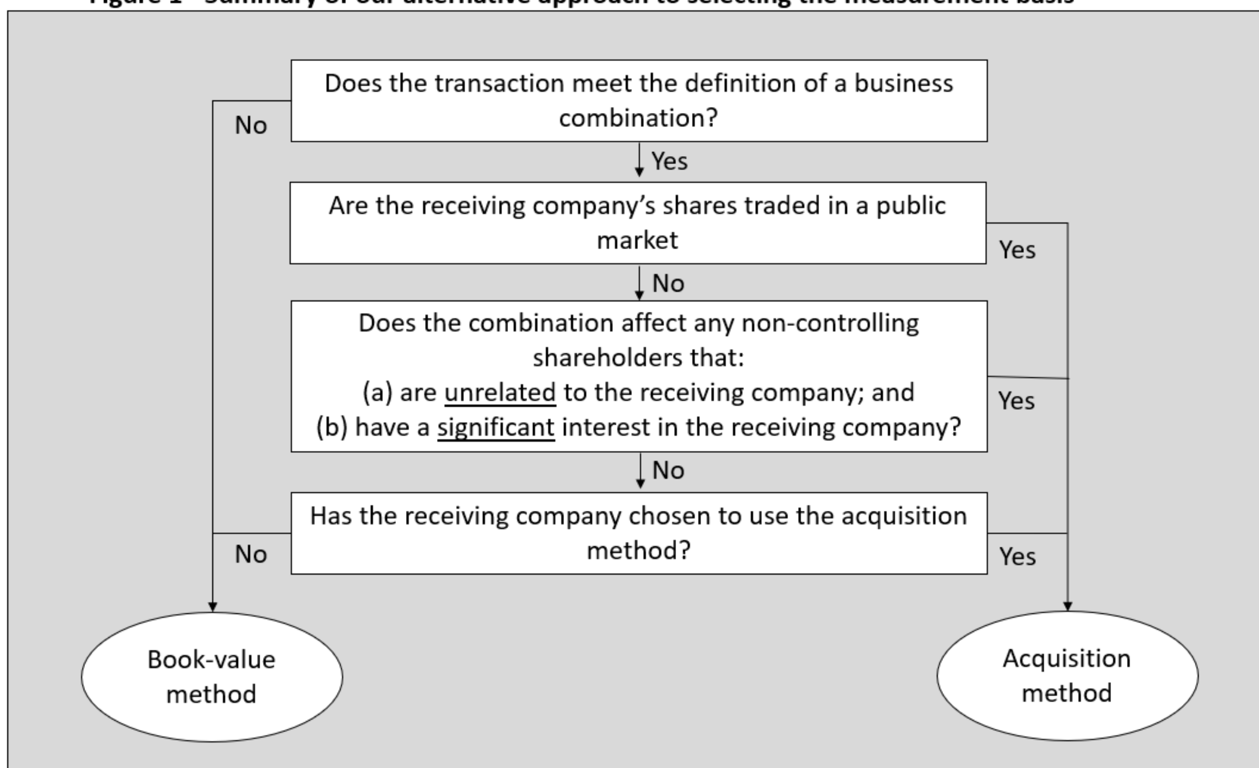
SELECTING THE MEASUREMENT BASIS

8. We acknowledge that there is no perfect solution to the dilemma of where to draw the line between which entities should apply the acquisition method and which should apply a book-value method. We do, however, disagree with a number of the Board's conclusions about which measurement basis should be used in which circumstances.
9. Our preferred approach for determining the measurement basis is summarised below:

Figure 1 - Summary of our alternative approach to selecting the measurement basis



10. This approach would require the acquisition method to be used by companies whose shares are listed on a public market and by those private companies with significant outside shareholders. Other entities would have an accounting policy choice between applying a book-value method and the acquisition method.
11. We accept that giving non-controlling interests a veto over the preparer's decision to apply a book-value method is one way of balancing costs, benefits and the information needs of shareholders. We do, however, have a number of conceptual and practical concerns about this proposal and are therefore not supportive of it. The need for a veto would also diminish if the model suggested above is applied as it would ensure that the information needs of significant outside shareholders are met by requiring the acquisition method to be used when such non-controlling interests exist.
12. See our answers to questions 2-4 below for more details.

APPLYING THE ACQUISITION METHOD

13. We are broadly supportive of the Board's preliminary views on applying the acquisition method. See our answer to questions 5 below for more details.

APPLYING A BOOK-VALUE METHOD

14. We are broadly supportive of the Board's preliminary views on applying a book-value method.
15. We have concerns, however, about a loss of information if pre-combination information is not restated, particularly when it comes to analysing trends over time, for example, where a business combination is undertaken in preparation for an initial public offering and where a

combination is effected by using a new parent company. We have some sympathy for this position but – at the same time – understand the logic behind the Board's preliminary views.

16. We suggest that the Board undertakes further outreach to determine if and in what circumstances it should allow or mandate retrospective restatement of pre-combination information.

17. See our answers to questions 6-10 below for more details.

DISCLOSURES

18. We are broadly supportive of the Board's preliminary views on disclosures. See our answers to questions 11-12 below for more details.

ANSWERS TO SPECIFIC QUESTIONS

Project scope

Question 1

Paragraphs 1.10–1.23 discuss the Board'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.

Do you agree with the Board's preliminary view on the scope of the proposals it should develop? Why or why not? If you disagree, what transactions do you suggest that the Board consider and why?

19. We broadly agree with the scope of the proposals as defined in paragraphs 1.10-1.23 of the discussion paper.

20. We note, however, that the project's scope includes group restructurings. Some group restructurings – such as where a business is transferred to a newly incorporated or shell company – will not meet the definition of a business combination and the Board should avoid creating confusion by labelling them as such. We recommend that the project is renamed to make it clear that it encompasses a wider range of transactions.

21. The discussion paper currently includes limited guidance on accounting specifically for group restructurings that do not meet the definition of a business combination. We believe that in many – possibly all – circumstances, a book-value approach should be applicable to such group restructurings, even when there are non-controlling interests in the receiving company.

22. Giving clear direction through application guidance could be a way to simplify the analysis required for these transactions and to address our concerns about potential confusion with transactions that are business combinations. Alternatively, such group restructurings could be spun off into a separate project if keeping them within scope is likely to cause delays to the long-awaited guidance on BCUCC.

Hive ups

23. The discussion paper does not directly address accounting for hive ups ie, group restructuring where the net assets of, and business undertaken by, a subsidiary are transferred up into the parent company. It is unclear whether such transactions are intended

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to be within the scope of the discussion paper and – if they are – how they should be accounted for. In particular, while a hive-up involves a transfer of a business to a parent, it is not clear that a receiving company has obtained control of that business (since it already controlled the business, through control of its subsidiary).

24. It is open to debate whether hive ups meet the definition of a business combination. As such we believe that they should generally be accounted for at book value, consistent with our observations in paragraph 68 below. We are, however, concerned, that applying the approach outlined in the discussion paper would require such transactions to be accounted for using the acquisition method where the parent company's shares are traded in a public market. Further clarity on this topic is needed.

Transitory control

25. In describing business combinations under common control, paragraph B1 of IFRS 3 *Business Combinations* requires that common control is not 'transitory' but does not provide guidance on that notion. We note that the Board has currently included transfers that are 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 within this project's scope. In some cases, such transfers may be part of an integral step plan or contractually linked. It is, however, hard to determine if and when such transactions should be within scope or what the full impact of the proposals will be until the Board clearly defines what is meant by 'transitory' control.

Other common control transactions

26. Appendix B of the discussion paper highlights some common control transactions that are outside of the project's scope, including the transfer of a company that does not have a business and the transfer of an investment in an associate. There is, however, diversity in how such transactions are currently accounted for. We therefore believe that these and other common control transactions should be addressed as part of a future project.

27. The scope of the discussion paper also excludes how a receiving company should report in its separate financial statements an investment in a subsidiary received in a BCUCC. We are not convinced that there is currently sufficient guidance on how such transactions should be accounted for and are aware of some diversity in practice. We believe that this issue should be addressed as part of a future project.

Interaction with IFRS 1

28. The discussion paper does not provide any discussion on the interaction between its preliminary views and paragraphs D16 and D17 of IFRS 1 *First-time Adoption of International Financial Reporting Standards.* It is not uncommon for individual companies of an IFRS 1 group reporter not to apply IFRS in their individual financial statements. However, a business combination under common control or a group restructuring can often lead to an entity within such a group needing to prepare IFRS financial statements for the first time. Clarity is needed, for example, over when a new company inserted to effect a group restructuring within an IFRS reporting group should be considered a first-time adopter and, if so, how it should first apply IFRS.

29. This issue is linked with the question over whether pre-transaction financial information, including comparatives, should be presented where a book-value method is applied and the extent to which the new reporting entity's financial statements are regarded as a continuation of the previous entity/business or, where applicable, one of the combining entities/businesses.

30. Similarly, the discussion paper does not provide any proposals on the interaction between its preliminary views and Appendix C of IFRS 1. Clarity is needed as to whether the 'grandfathering' exemptions provided by this appendix – which currently only apply to

business combinations within the scope of IFRS 3 – will be available to entities applying the acquisition method consequent to any future standard on BCUCC.

31. The Board may also wish to consider whether any relief should be available to first-time adopters from restating transactions – including group restructurings that are not business combinations – that would be accounted for using a book-value method under any future standard.

32. In some cases, a BCUCC or group restructuring that is not a business combination may take place many years before the reporting entity is required to prepare IFRS financial statements. Retrospective restatement in such circumstances could be very onerous unless adequate relief from this requirement is provided.

Selecting the measurement method

Question 2

Paragraphs 2.15–2.34 discuss the Board'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 (see Question 3).

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?

One size doesn't fit all

33. We agree with the Board's conclusion that one size doesn't fit all and that some BCUCC should be accounted for using the acquisition method and that others should be accounted for using a book-value method. The situations in which such business combinations occur are many and various and it is therefore appropriate that differences arise in the accounting used to report them.

34. We agree that the accounting in this area should be driven by user needs. Just as the situations in which BCUCC occur are many and various so too are the needs of users of financial information relating to these transactions. The Board's preliminary views acknowledge these differing needs and accept that the method used should depend on the circumstances.

35. While we are supportive of the Board's attempts to reduce the current diversity in practice, we do not fully support the proposals set out in the discussion paper.

Restructurings that do not meet the definition of a business combination

36. As noted in paragraphs 21-22 above, the discussion paper currently includes limited guidance on accounting for group restructurings that do not meet the definition of a business combination. Any future standard needs to provide clear guidance in this area to avoid confusion and potential diversity in practice. We believe that in many – possibly all – circumstances, such transactions should be accounted for using a book-value method.

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Listed companies

37. We agree that the acquisition method should be applied if the company's shares are traded in a public market (with the exception of hive-ups as discussed in paragraph 24). See paragraph 50 below for more details.

Unlisted companies with non-controlling shareholders

38. We also agree, in principle, that the acquisition method should be applied if the transaction meets the definition of a business combination and affects non-controlling shareholders of the receiving company. These non-controlling shareholders have acquired an ownership interest in the transferred company and their information needs are similar to equivalent shareholders in transactions within the scope of IFRS 3.

39. Our preferred approach is, however, slightly different to the Board's preliminary views. Having considered the costs and benefits of applying the acquisition method, we believe that it should be mandated for companies whose shares are not traded on a public market when the combination affects non-controlling shareholders that:
    - are unrelated[1] to the receiving company; and
    - have a significant interest in the receiving company.

40. Such an approach acknowledges the information needs of non-controlling shareholders while recognising that the costs of applying the acquisition method are unlikely to be justified where such shareholders have an 'insignificant' ownership interest in the receiving company. Similar to the Board's own proposals, it also acknowledges that those costs are unlikely to be justified when all non-controlling shareholders are related parties of the receiving company who may not need to rely on the company's financial statements to meet their information needs.

41. Adopting our suggested approach would, of course, require the Board to give guidance on determining when an interest is 'significant'. Such guidance should make it clear that significance relates only to the size of the non-controlling interest and that this is measured relative to the receiving entity rather than the non-controlling shareholder. We acknowledge that setting a quantitative threshold to define what is meant by 'significant' would be arbitrary and lack a conceptual basis. Instead, we suggest that the determination of what qualifies as a 'significant' interest is left to the preparer's judgement.

Accounting policy choice

42. Where the non-controlling shareholders do not meet the criteria set out in paragraph 39 above, we suggest that entities should have an accounting policy choice between applying a book-value method and the acquisition method.

43. We believe that in such circumstances a book-value method should normally be the most appropriate accounting policy choice but accept that in some circumstances the acquisition method may be more appropriate.

44. It may, for example, be appropriate to apply the acquisition method to business combinations where the price paid is similar to what one would expect in an arm's length transaction, especially if there are unrelated non-controlling shareholders, even if their holdings are not significant.

45. We suggest that the Board undertakes more analysis to identify circumstances in which applying the acquisition method would be appropriate. Application guidance outlining such circumstances would help guide preparers when applying their judgement and help to ensure that similar transactions are accounted for consistently.

[1] Meaning an entity that is not a related party as defined by IAS 24 *Related Party Disclosures*

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NCI objection to book-value

46. As noted in paragraphs 38-45 above, we believe that privately held companies should be required to apply the acquisition method when there are unrelated non-controlling shareholders with a significant interest in the receiving company and that entities should have an accounting policy choice between a book-value method and the acquisition method in other circumstances. If such a model was adopted, we believe that it would be inappropriate to give non-controlling interests – particularly those with 'insignificant' shareholdings – a veto over the preparer's decision to apply a book-value method.

47. Moreover, we have a number of conceptual and practical concerns about the Board's suggestion that non-controlling shareholders should be contacted and given the opportunity to object to the use of a book-value method. These are discussed in our response to question 3 below.

Unlisted companies with no outside shareholders

48. Where the combination is between wholly-owned entities, many preparers currently choose to apply a book-value method. We believe that this will be appropriate in most circumstances. We do not, however, agree with the Board's conclusion that this method should be mandated for such entities and that the approach discussed in paragraphs 42-45 above may be more appropriate.

49. Moreover, creating a 'bright line' between when the acquisition method must be used and when a book-value method must be used that is dependent solely on the existence of non-controlling shareholders risks creating structuring opportunities.

Question 3

Paragraphs 2.35–2.47 discuss the cost–benefit trade-off and other practical considerations for business combinations under common control that affect non-controlling shareholders of the receiving company.

(a) In the Board's preliminary view, the acquisition method should be required if the receiving company's shares are traded in a public market.

Do you agree? Why or why not?

(b) In the Board's preliminary view, if the receiving company's shares are privately held:

(i) the receiving company should be permitted to use a book-value method if it has informed all of its non-controlling shareholders that it proposes to use a book-value method and they have not objected (the optional exemption from the acquisition method).

Do you agree with this exemption? Why or why not? Do you believe that the exemption will be workable in practice? If not, in your view, how should such an exemption be designed so that it is workable in practice?

(ii) the receiving company should be required to use a book-value method if all of its non-controlling shareholders are related parties of the company (the related-party exception to the acquisition method).

Do you agree with this exception? Why or why not?

(c) If you disagree with the optional exemption (Question 3(b)(i)) or the related-party exception (Question 3(b)(ii)), in your view, how should the benefits of applying the acquisition method be balanced against the costs of applying that method for privately held companies?

Listed companies vs. unlisted companies

50. We agree that the acquisition method should always be applied where the transaction meets the definition of a business combination and the receiving company's shares are traded in a

public market as this will reduce diversity in practice. Moreover, in such instances there will generally be a significant and widely dispersed non-controlling interest whose information needs will be best met by applying the acquisition method. It may be appropriate to extend this requirement to BCUCC undertaken by a company in the process of listing some of its shares in the near future, especially as transfers that are conditional on a sale of the combining companies to an external party, such as in an initial public offering, are stated to be within scope.

51. We agree that in many instances a book-value method should be applied where the receiving company's shares are privately held. As discussed in response to question 2 above, our proposal would not permit this where there are significant outside shareholders.

Unlisted companies – the optional exemption from the acquisition method

52. We are not supportive of the proposals to give non-controlling interests a veto over the preparer's decision to apply a book-value method. If, however, the Board decides to continue with this approach, more clarity is needed on when and how this veto can be applied:
    - The discussion paper focuses on receiving companies with simple capital structures, comprising only ordinary shares that meet the definition of an equity instrument and simple debt instruments that meet the definition of a liability. However, the glossary of the discussion paper makes it clear that other equity instruments – as defined by IAS 32 *Financial Instruments: Presentation* – need to be considered when assessing non-controlling interests. Clarity over the treatment of more complex instruments will be needed in the next phase of the project, including transparency over whether or not the holders of put options over ordinary shares, which are classified as liabilities, should be considered to be non-controlling shareholders. In our view, it may be appropriate to limit the definition of non-controlling shareholders for the purposes of any future standard to those with a present ownership interest that entitle their holders to a proportionate share of the entity's net assets in the event of liquidation, as per paragraph 19 of IFRS 3.
    - The discussion paper does not acknowledge that any objection to the use of a book-value method has a fundamental impact on the accounting for the business combination in all future sets of financial statements. It seems inappropriate for the accounting for a business combination to be dictated by the action of the non-controlling shareholder base at a particular point in time. The proposals do not consider the information needs of potential future shareholders. This differs from the existing exemption from preparing consolidated financial statements – which contains a similar non-controlling objection – as in that case shareholders can decide whether or not they wish to object each financial year.
    - There are also practical difficulties around determining whether the non-controlling shareholders object to the use of a book-value method. Clarity is needed, for example, on how and in what form non-controlling shareholders should be notified, on whether they would be expected to object in a certain way, within a particular timeframe, and on whether silence can be assumed to indicate consent.
    - The proposal also raises issues about governance ie, is it appropriate for a small number of potentially uninformed shareholders – or even a single shareholder – to veto the directors' selection of an accounting policy? It seems particularly odd that, for example, a company with 100 non-controlling shareholders could be obliged to use the acquisition method if one shareholder objected, even if the other 99 were content with using a book-value method. If the Board were to proceed with their proposals, introducing a *de minimis* threshold stating that objections must be lodged from a certain

percentage of shareholders before the acquisition method is required could overcome this problem.

Unlisted companies – the related-party exception to the acquisition method

53. We agree that a book-value method may be more appropriate where all of the receiving company's non-controlling shareholders are related parties of the company. We do not, however, agree that such an approach should be mandated in all circumstances and that the approach discussed in paragraphs 42-45 above may be more appropriate.

54. If the Board decides to require the use of a book-value method where all of the receiving company's non-controlling shareholders are related parties of the company, it should clearly explain why the acquisition method is never appropriate in such circumstances.

Question 4

Paragraphs 2.48–2.54 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 Board'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?

55. We agree that these exemptions should not be available to publicly traded receiving companies.

56. Extending the optional exemption from the acquisition method to publicly traded receiving companies would be inappropriate as shareholders in such companies rely on the information provided from acquisition accounting. Moreover, extending the optional exemption to them would be difficult in practice as such companies typically have a large and frequently changing number of non-controlling shareholders. Consequently, it would be difficult to obtain the consent required.

57. Extending the related-party exception to publicly traded receiving companies would have very limited – if any – application in the UK as it is unlikely that all non-controlling shareholders of a publicly-traded company will be related parties.

Applying the acquisition method

Question 5

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

(a) In the Board'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 Board'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 Board 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?

58. We understand the Board's reasons for not developing a requirement for the receiving company to identify, measure and recognise a distribution from equity when applying the acquisition method to a BCUCC. We are, however, concerned that including any 'overpayment' in goodwill may result in the recognition of an asset that does not meet the definition included in the conceptual framework and that any subsequent impairment of that asset may not reflect the substance of the transaction, being a distribution in equity. In cases where the goodwill is tested for impairment at a higher cash generating unit, there may not even be an impairment in respect of the 'overpayment' in goodwill.

59. We agree that splitting the 'overpayment' between a distribution from equity and goodwill is likely to be both complex and judgemental as in many cases it will be difficult to determine what a third party would have paid in an equivalent combination. In some instances, however, a BCUCC and a distribution may be bundled together as part of a single transaction. We believe that the Board should either make it clear that unbundling the distribution will be appropriate in some circumstances or explain why this is not necessary given the existing guidance on determining what is part of the business combination transaction in IFRS 3 paragraphs 51-53 and B50-B62B. We welcome the proposed additional disclosures about the terms of the business combination, including how the transaction price was set.

60. We agree that the receiving company should recognise any 'underpayment' as a contribution to equity rather than as a bargain purchase gain. As above, separating out the notional bargain purchase gain from the equity contribution is likely to be difficult in practice. If this disaggregation is to be avoided, we believe that it is better to recognise the full amount as an equity contribution rather than as a gain in profit or loss.

61. More guidance is needed on identifying the acquirer as this can be challenging in common control situations, particularly where a NewCo is used. Indeed, paragraph 2.27 of the discussion paper acknowledges that identifying the acquirer in a business combination under common control involving wholly-owned companies might be difficult, although similar issues may also arise where there are non-controlling shareholders. Paragraph B18 of IFRS 3 prohibits a NewCo issuing shares from being identified as the acquirer, but there is currently limited guidance in IFRS 3 on in what circumstances a NewCo could be the acquirer where the acquisition is effected by paying cash or incurring liabilities. In practice, a NewCo is rarely identified as an acquirer in a BCUCC, although paragraph 2.26 of the discussion paper suggests it would be possible to identify a NewCo as an acquirer in a transaction involving wholly-owned group companies. However, some BCUCC may be a prelude to external transactions where a NewCo paying cash or incurring liabilities might have more substance. Enhanced guidance is critical to reduce diversity in practice. This is particularly important given use of the acquisition method would be expected to be more prevalent under the discussion paper's proposals in the context of BCUCC.

Applying a book-value method

Question 6

Paragraphs 4.10–4.19 discuss the Board'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 Board's preliminary view? Why or why not? If you disagree, what approach do you suggest and why?

Business combinations under common control

62. When applying a book-value method to a business combination under common control, the receiving company will typically measure the assets and liabilities received at either:
    - the transferred company's book values; or
    - the controlling party's book values ie, the amounts included in the consolidated financial statements of the transferred company's parent or ultimate parent.
63. Some argue in favour of the former as it provides uninterrupted historical information about the transferred company that is useful in analysing trends. But the transferred company may not prepare IFRS financial statements and creating book values on such a basis for the first time may be both time consuming and costly.
64. Others prefer the latter approach, as it involves using a more recent valuation of the transferred company's assets and liabilities that the shareholders of the parent or ultimate parent are more familiar with. But it isn't always straightforward as in some instances it is unclear whose consolidated book values should be used, where consolidated IFRS financial information is prepared at the level of both the ultimate and a lower parent.
65. There are certainly pros and cons to both approaches and those on either side of the debate will undoubtedly contend that their preferred option provides the most decision-useful information for financial statement users.
66. While a case can be made for either approach, continuing to allow an accounting policy choice in this area would not meet the Board's objective of reducing diversity in practice. We therefore agree that any future standard should allow only one of these approaches for accounting for business combinations under common control. Having considered the arguments put forward in the discussion paper we agree that, on balance, using the transferred company's book values is more appropriate than using the controlling party's book values.
67. Further guidance would, however, be helpful as it is unclear whether or not there is a new initial point of recognition when the assets and liabilities are initially recognised in the receiving company's financial statements. A simple example of this is determining whether the value of property, plant & equipment and the associated accumulated depreciation is recognised in receiving company's financial statements or just the net book value. Similar – but more complex issues – may also arise in relation to certain financial instruments, hedging, deferred tax and other matters. There may also be issues around determining whether certain items in other comprehensive income should be reclassified to profit or loss. More detail is needed to avoid diversity in practice. We suggest that the Board undertakes further analysis and outreach on these matters.

Group restructurings that are not business combinations

68. As mentioned previously, the discussion paper provides little analysis of accounting for group restructurings that are not business combinations. We believe that in many – possibly all – circumstances, a book-value approach should be applicable to such group restructurings. More research is, perhaps, needed to determine how the receiving company should measure

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the assets and liabilities received in such transactions. We suggest that the Board undertakes more outreach to determine whether there are any circumstances where it would be appropriate to account for group restructurings using the acquisition method.

Question 7

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

(a) the Board 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.

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

Consideration paid in own shares

69. The reporting of components within a reporting company's equity and the measurement of issued shares for the purpose of that reporting are often affected by national requirements and regulations. We therefore agree that the Board should not prescribe how the receiving company should measure any consideration paid in its own shares when applying a book-value method.

Consideration paid in assets

70. We agree with the Board's preliminary view that consideration paid in assets should be measured at the receiving company's book values of those assets at the combination date. This approach is consistent with a model that focuses on book values and is likely to be less costly than measuring the consideration paid in assets at their fair values. Moreover, it avoids any gain or loss on derecognition being recognised in the receiving company's statement of profit or loss.

71. The Board's proposals are, however, inconsistent with the IFRS Interpretation Committee's January 2013 agenda decision on accounting for the purchase of a non-controlling interest by the controlling shareholder when the consideration includes non-cash items which concluded that any gain or loss arising on derecognition should be recognised in profit or loss. Notwithstanding this discrepancy, we remain supportive of the Board's proposals.

Consideration paid by incurring or assuming liabilities

72. We agree with the Board's preliminary view that consideration paid by incurring or assuming liabilities should be measured at the amount determined on initial recognition of the liability at the combination date as we believe that this approach provides the most useful information about those liabilities and avoids a day two measurement issue.

Question 8

Paragraphs 4.44–4.50 discuss the Board'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 Board should not prescribe in which component, or components, of equity the receiving company should present that difference.

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

73. In practice, when applying a book-value method, the receiving company typically recognises any difference between the consideration paid and the book value of the assets and liabilities received in equity. The alternative of disaggregating this difference into its component parts and accounting for them accordingly is likely to be costly and complex to apply. We therefore agree with the Board's preliminary views.

74. We also agree that the Board should not prescribe whereabouts in equity the receiving company should present that difference for the reasons discussed in paragraph 69 above.

Question 9

Paragraphs 4.51–4.56 discuss the Board's preliminary view that, when applying a book-value method to a business combination under common control, the receiving company should recognise transaction costs as an expense in the period in which they are incurred, except that the costs of issuing shares or debt instruments should be accounted for in accordance with the applicable IFRS Standards. Do you agree with the Board's preliminary view? Why or why not? If you disagree, what approach do you suggest and why?

75. The Board's preliminary view is consistent with what generally occurs in practice when entities apply a book-value method. Moreover, the proposals are consistent with IFRS 3's approach to accounting for transaction costs when the acquisition method is used. We see no reason why such costs should be treated differently when a book-value method is used. We are therefore supportive of the Board's preliminary views.

Question 10

Paragraphs 4.57–4.65 discuss the Board'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 Board's preliminary view? Why or why not? If you disagree, what approach do you suggest and why?

The current UK approach

76. When applying a book-value method, UK companies often combine the assets, liabilities, income and expenses of the transferred company retrospectively ie, the receiving company's financial statements are prepared as if the combining companies had always been combined, with pre-combination information restated from the beginning of the earliest period presented.

77. This approach was part of the now withdrawn UK standard FRS 6 *Acquisitions and Mergers* and has since been incorporated into FRS 102 *The Financial Reporting Standard applicable in the UK and Republic of Ireland*. Many UK companies adopting IFRS have continued to apply this approach in the absence of any guidance within IFRS standards on BCUCC and other group restructurings. It is commonly used under IFRS where restructurings are undertaken in preparation for an initial public offering and where they are effected by using a new parent company.

Business combinations under common control

78. Moving to a prospective basis of accounting for BCUCC will therefore, perhaps inevitably, meet with some resistance from UK constituents. There are anxieties about a loss of information if pre-combination information is not restated, particularly when it comes to analysing trends over time. There are also concerns about the impact this will have on the preparation of historical information in prospectuses and accountants' reports thereon. We have some sympathy for this position but – at the same time – understand the logic behind the Board's preliminary views.

79. We would not support mandating the restatement of pre-combination information for BCUCC as in some instances doing so would be both impractical and costly. It may, therefore, be better for the Board to allow companies to choose to retrospectively restate pre-combination information where the facts and circumstances suggest that doing so would be appropriate. In other words, it may be better to allow entities to weigh the costs and benefits of restating and to apply their own judgement when deciding which approach is appropriate in their circumstances. The alternative of not allowing a choice to restate would, perhaps, be a proliferation of non-GAAP pro-forma information outside of the primary financial statements which the Board may find undesirable.

80. We suggest that the Board undertakes further outreach to determine if and in what circumstances it should allow or mandate retrospective restatement of pre-combination information.

Group restructurings that are not business combinations

81. As mentioned previously, the discussion paper provides little analysis of accounting for group restructurings that are not business combinations.

82. In some instances – such as where a business is transferred to a NewCo immediately prior to an initial public offering – a potential loss of pre-combination information is worrying. We suggest that the Board undertakes more outreach to determine whether it is appropriate to require restatement of pre-combination information in such circumstances.

Disclosure requirements

Question 11

Paragraphs 5.5–5.12 discuss the Board'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 Board 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 Board's preliminary views? Why or why not? If you disagree, what approach do you suggest and why?

83. We agree with the Board's preliminary view that IFRS 3's disclosure requirements – and any of the possible improvements to those requirements – should also apply to BCUCC when the acquisition method is used as the information needs of users are similar for all business combinations regardless of whether or not they are under common control.

84. We also agree that the additional application guidance on how to apply those disclosure requirements and those of IAS 24 to BCUCC would be helpful. However, we believe that the

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requirements of IAS 24 are equally relevant to transactions accounted for under a book-value method and that the application guidance should be extended to cover such transactions.

85. If the Board were to adopt the model we propose, some entities would be making significant judgements in determining whether a non-controlling interest is or isn't significant or whether the acquisition method or a book-value method should be applied. If the Board were to follow our recommendations in paragraphs 42-45 above, any future standard should emphasise that these judgements would need to be disclosed under paragraph 122 of IAS 1 *Presentation of Financial Statements.*

Question 12

Paragraphs 5.13–5.28 discuss the Board'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);***
- ***(b) the Board 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 Board's preliminary views? Why or why not? If you disagree, what approach do you suggest and why?

86. We broadly support the proposed disclosure requirements for BCUCC accounted for using a book-value method. Investors are often unhappy with the level of disclosures currently given and the additional information would be welcomed widely. As noted in paragraph 84 above, we believe that additional application guidance on how disclosure requirements for transactions accounted for under a book-value method are applied together with those of IAS 24 to BCUCC would be helpful.

87. See our answer to question 10 above regarding the restatement of pre-combination information.