

# Business Combinations under Common Control

Agenda ref 8A

Slide deck ①

*Scope of the project*

ASAF Meeting – December 2017

# Meeting agenda

**Agenda ref 8A**

**Scope of  
the project**

Slide deck **1**

**Agenda ref 8B**

**Methods of  
accounting**

Slide deck **2**



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<b>Project</b>	<b>Business Combinations under Common Control (BCUCC)</b>		
<b>Paper topic</b>	Scope of the project		
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# Overview of Slide deck ①

## Content

- 2014 tentative decision on the scope (slides 6-9)
- Clarifying the scope of the project:
  - Group restructurings (slides 13-22)
  - Business combinations vs BCUCC (slides 24-30)
- Illustrations of transactions within the scope (slides 32-37)
- Discussion (slide 39)

## Objective

The objective of the session is to seek your views on the scope of the project



# 2014 tentative decision on the scope

# 2014 tentative decision on the scope

- The Board tentatively decided that the project should consider:
  - business combinations under common control that are currently excluded from the scope of IFRS 3;
  - group restructurings; and
  - the need to clarify the description of business combinations under common control, including the meaning of ‘common control’.
- The Board also tentatively decided to **give priority to considering transactions that involve third parties**, for example those undertaken in preparation for an IPO. However, the Board did not restrict the scope of the project to such transactions only.
- The Board did not discuss which **reporting entity** and which **financial statements** of that reporting entity the project will focus on.

# Considerations in setting the scope

- In setting the scope of the project, the Board considered:



# Interaction with other Standards

	Transactions NOT under common control	Transactions under common control
NOT involving transfer of a business	Covered by applicable IFRS Standards	Covered by applicable IFRS Standards (scope exclusion do not apply)
involving transfer of a business	Covered by IFRS 3	Not covered by IFRS Standards

The staff will consider interaction with accounting for other transactions under common control as the project progresses (eg acquisition of associates, see next slide)

The staff will consider interaction with accounting for business combinations NOT under common control as the project progresses



# Related IC topics—scope exclusions

In 2017 the IFRS Interpretation Committee (IC) discussed:

- **can IFRS 3 scope exclusion for BCUCC be applied by analogy to other transactions under common control?**
  - IC tentative Agenda Decision—unless a Standard excludes transactions under common control from its scope, an entity applies the requirements in the Standard to those transactions.
- **how to account for an acquisition of an associate or of an interest in a joint venture under common control?**
  - the IC considered whether to apply the requirements in IAS 28 or the IFRS 3 scope exclusion for BCUCC;
  - the IC did not finalise its tentative Agenda Decision;
  - the staff will consider interaction between BCUCC and requirements in IAS 28 as the project progresses.

# Clarifying the scope of the project

# Clarifying the scope of the project

**Group  
restructurings**  
(slides 12-21)



**Not a defined term**, and  
its meaning not described  
in IFRS Standards



**Discussed  
at the October 2017  
IASB meeting**

**BCUCC**  
(slides 23-29)



Described in IFRS 3, but  
there are **application  
questions**



**Planned for discussion  
at the December 2017  
IASB meeting**

# Clarifying the scope of the project Group restructurings

# Group restructurings

- The 2014 Board's tentative decision referred to group restructurings.
- However, '**group restructuring**' is not a defined term and is used differently by different parties.



# Staff analysis (1/4)

## ‘restructuring’

... organising components of the whole in a different way

## in a group

... organising **entities or business** within the group in a different way

Such changes in the group structure would involve **transferring entities or businesses between existing or newly created entities under common control**. Some such transfers would satisfy the description of BCUCC whereas others would not.

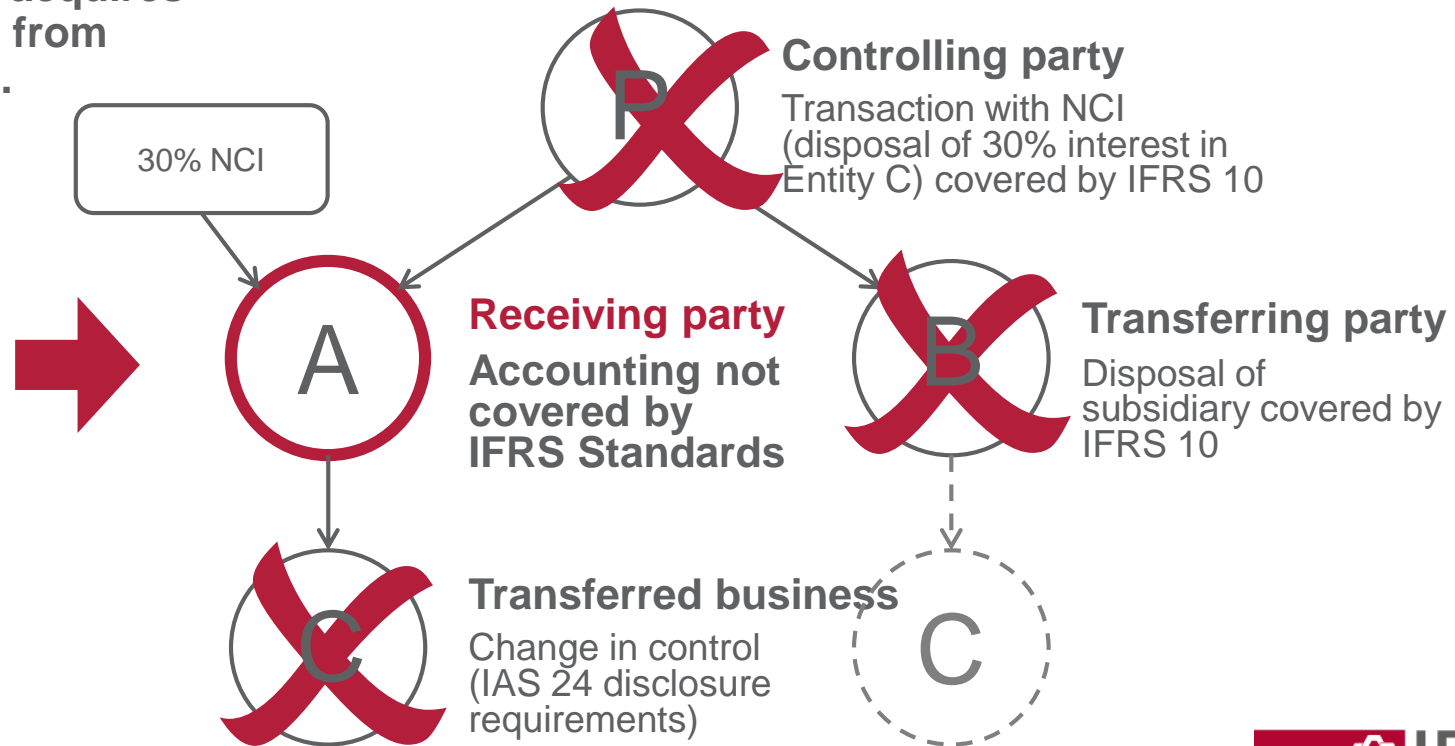
# Staff analysis (2/4)

- To identify and describe the population of transactions that should be included in the scope of the project, the staff analysed a broad group of transactions that involve restructuring the relationships between entities or businesses under common control.
- The staff noted that regardless of whether a transfer of an entity or business within a group satisfies the description of a business combination under common control, any such transfer would involve the following parties:
  - **the controlling party or parent;**
  - **the transferring party;**
  - **the transferred party (entity or business); and**
  - **the receiving party.**

# Staff analysis (3/4)

- Accordingly, a transfer of an entity or a business within a group can be analysed from the point of view of the parties involved in the transaction:

Entity A acquires  
Entity C from  
Entity B.





# Staff analysis (4/4)

- A transfer of an entity or a business under common control may or may not satisfy the description of a BCUCC:
  - **if one of the combining parties can be identified as the acquirer** if IFRS 3 were applied, the transaction satisfies the description of a BCUCC and is included in the scope of the project in accordance with the Board's 2014 tentative decision;
  - **if none of the combining parties can be identified as the acquirer** if IFRS 3 were applied, the transaction is not a BCUCC. However, accounting for such transactions is not addressed in IFRS Standards.

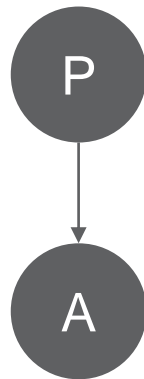
# Related IC topics—one business (1/2)

IC submission—2011

- In **2011** the IC discussed a transaction where a Newco is established to acquire **one** other entity or business under common control.

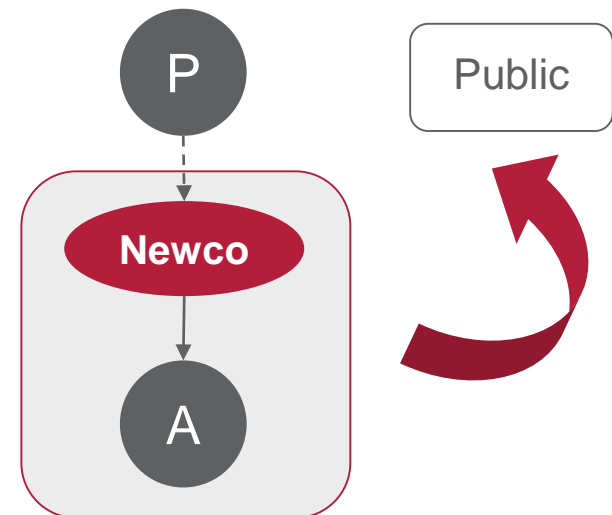
## Before

Entity A is controlled and fully owned by Entity P. Entity P wants to sell Entity A through an IPO using a Newco.



## After

Newco issues new shares to acquire Entity A. Possibly Newco will raise new capital from public shareholders; however a period of several months may lapse.



## Related IC topics—one business (2/2)

- The transaction in question is **not a BCUCC** because it **does not meet the definition of a ‘business combination’**:
  - Newco cannot be identified as the acquirer according to IFRS 3.B18;
  - Entity A cannot be identified as the acquirer either, because Newco does not meet the definition of a business.
- The IC decided that this topic would be better considered within the context of a broader project on accounting for common control transactions and did not add the topic to its agenda.

# 2017 Board's clarification

The Board tentatively decided that the BCUCC project will address accounting for transactions under common control in which the reporting entity obtains control over one or more businesses, **regardless of whether IFRS 3 would identify the reporting entity as the acquirer if IFRS 3 were applied.**



According to the 2017 Board's clarification of the scope, the transaction discussed in the 2011 IC submission (slide 18) is included in the scope of the project.

# Which financial statements? (1/2)

- In 2014, the Board **did not discuss which financial statements**—consolidated, separate or individual—the BCUCC project will focus on.
- In 2017, the Board decided that the **project will focus on the transactions** that the reporting entity needs to account for.

Which financial  
statements?



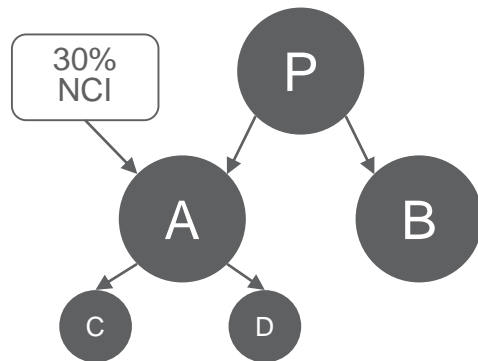
The scope will not specify **to which financial statements** of that reporting entity any accounting requirements developed in the project will apply.

This is because **the financial statements affected by any accounting requirements developed in the BCUCC project will depend on specifics of the transaction** (*see the example on next slide*).

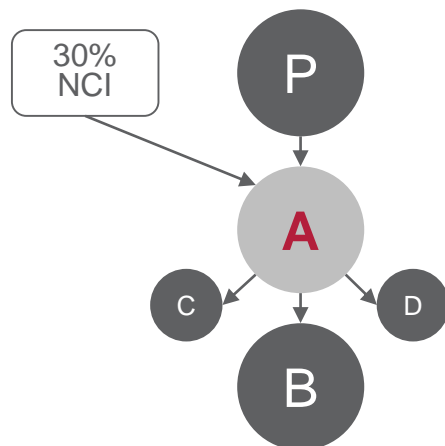
This is also **consistent with** how the scope is set out in **IFRS 3**.

# Which financial statements? (2/2)

## Transaction



Entity A acquires business B from Entity P.



## B = separate entity

- ✓ Any requirements developed in the BCUCC project will apply in Entity A **consolidated** financial statements.
- ✓ In Entity A **separate** financial statements, it will account for its investment in entity B applying IAS 27 *Separate Financial Statements*.

## B ≠ separate entity

- ✓ Any requirements developed in the BCUCC project will apply in **all financial statements prepared** by Entity A (consolidated or separate).

# Clarifying the scope of the project BCUCC

# Description of BCUCC

- **BCUCC are business combinations in which all the combining entities or businesses are ultimately controlled by the same party or parties both before and after the business combination, and that control is not transitory (IFRS 3.B1).**
- The key components of this description are:

**transaction is a  
'business combination'**



**IFRS 3 defines 'business combination'**



**all the combining entities are  
'under common control'**



**IFRS 3.B2-B4 provide application guidance on how to assess 'common control'**



**the common control is  
'not transitory'**

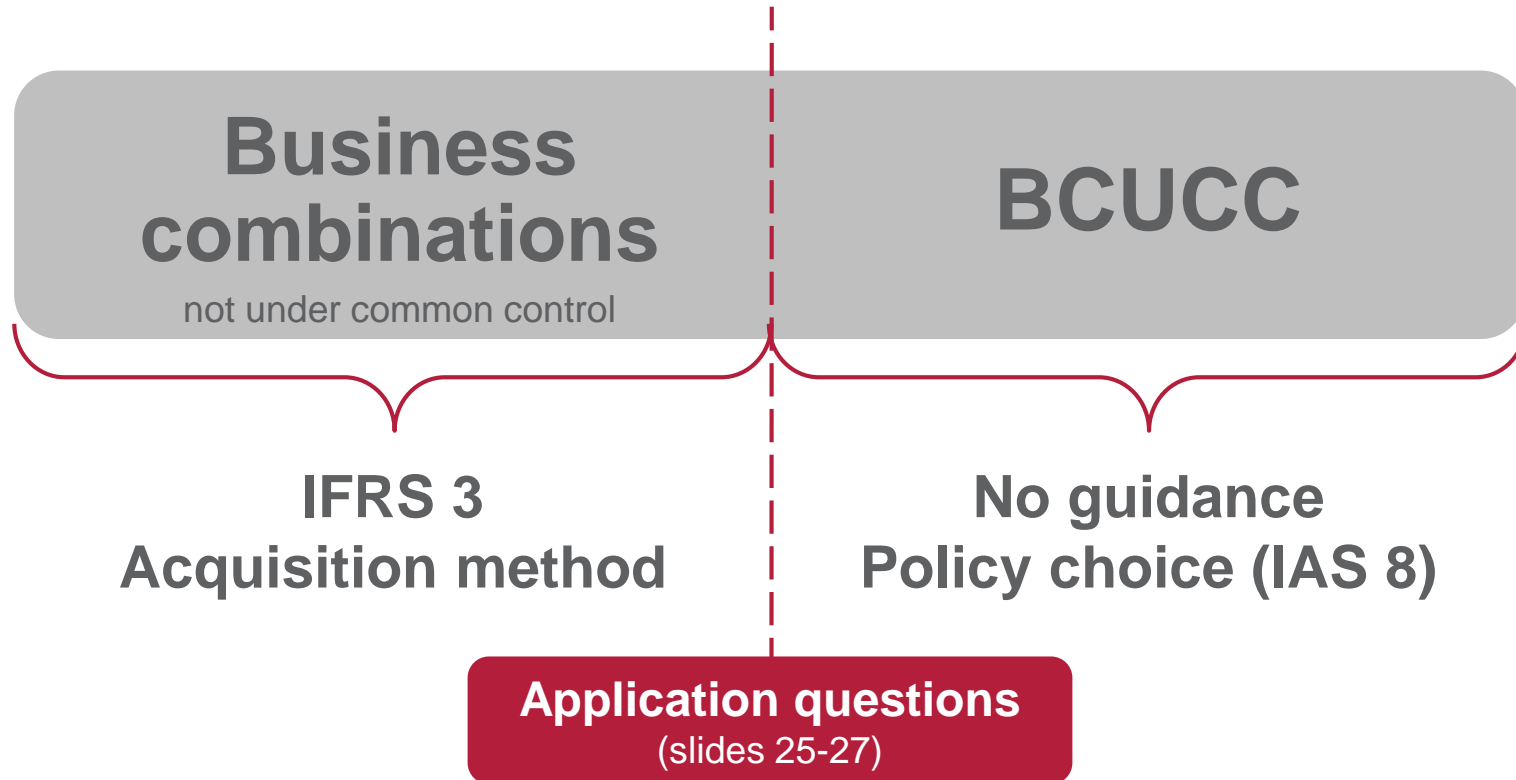


**IFRS 3 does not elaborate on 'transitory control'**





# Business combinations vs BCUCC



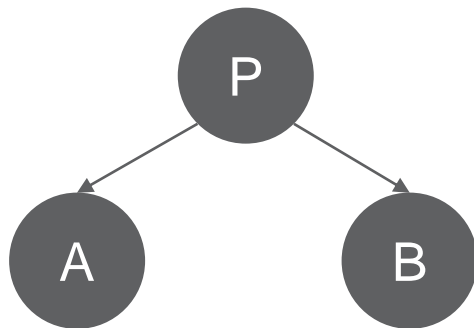
- Transitory control?
- Conditional IPO?
- ...

# Related IC topics—transitory control (1/2)

- In 2006 the IC considered whether a **group restructuring involving a formation of a new entity** to facilitate the sale of a part of the group (eg in an IPO) is a business combination within the scope of IFRS 3.

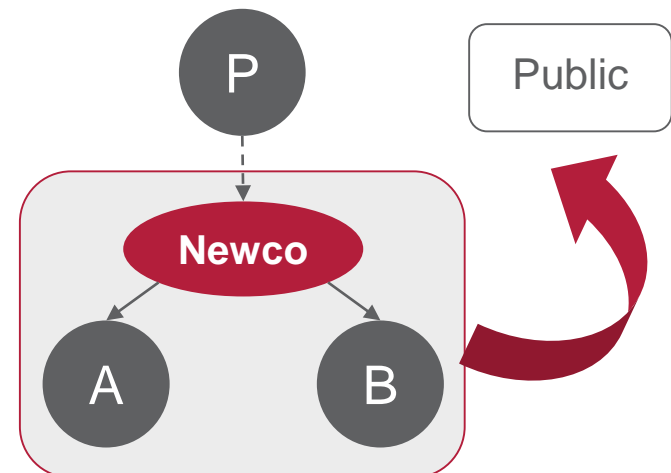
## Before

Entity A and Entity B are controlled and fully owned by Entity P; Entity P wants to sell A and B through an IPO using a Newco.



## After

In preparation of the IPO, Entity P formed a Newco and transferred Entity A and Entity B to that Newco.



## Related IC topics—transitory control (2/2)

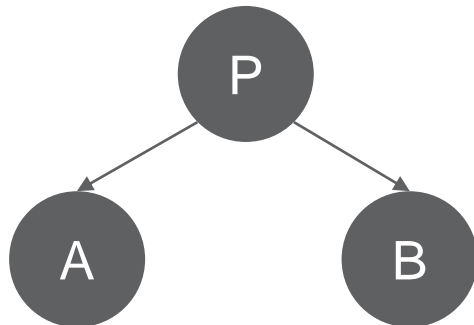
- Some argued that **control of the new entity is transitory** and therefore a combination involving a newly formed entity is a business combination within the scope of IFRS 3.
- The IC concluded that the consideration of common control applies to the **combining entities that existed before the combination, excluding the new entity.**
- The IC decided not to add this topic to its agenda.

## Related IC topics—conditional IPO (1/2)

- In **2011** the IC discussed a transaction where a newly formed entity (Newco) is established to acquire other entities under common control for cash raised in an IPO **and the acquisition is conditional on the occurrence of the IPO** (the IPO results in a loss of control of Newco).

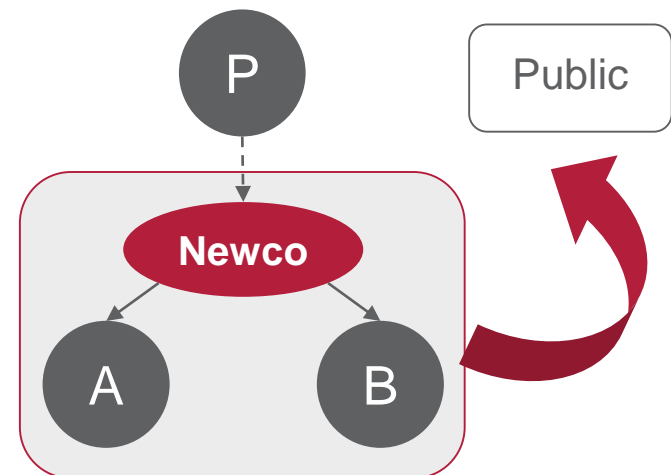
### Before

Entity A and Entity B are controlled and fully owned by Entity P; Entity P wants to sell A and B through an IPO using a Newco.



### After

Entity P formed a Newco. **Newco will acquire Entity A and B only on condition of the occurrence of Newco IPO.**

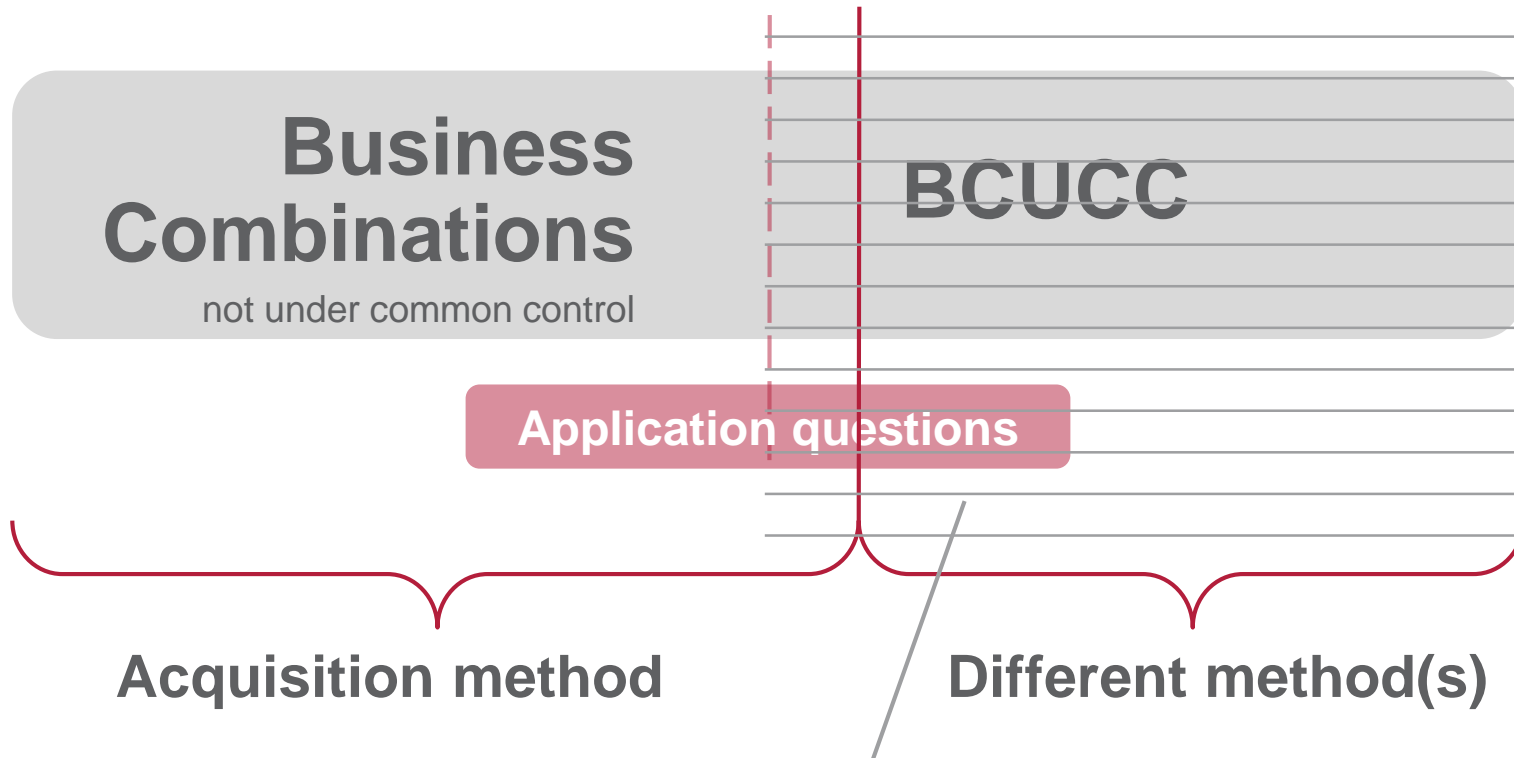


## Related IC topics—conditional IPO (2/2)

- Regarding the example on the previous slide:
  - ① some argue that **the IPO takes place before the acquisition**, hence Entity P does not control Newco at the time of the acquisition, therefore **the acquisition is NOT a BCUCC**;
  - ② others argue the **acquisition happens before the IPO**. This would mean that Entity P controls Newco, Entity A and B at the time of the acquisition. However, there are **different views as to whether Entity P's control** over Newco, Entity A and Entity B is **transitory**:
    - if **YES—transitory control**      ➔ **NOT a BCUCC**
    - if **NOT—control not transitory**      ➔ **BCUCC**
- The IC decided that this topic would be better considered within the context of a broader project on accounting for common control transactions and did not add the topic to its agenda.

# Staff recommendation

Application questions focus on the distinction between BC and BCUCC...



## Staff recommendation on scope of BCUCC project

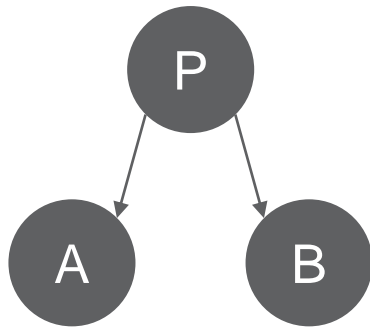
'Fill in the gap' in accounting for business combinations, instead of focussing on the distinction between BC and BCUCC.

# Illustrations of transactions within the scope

# Example 1—Basic

## Before

Entity A and Entity B are controlled by Entity P.  
Entity B is a business.



## After

Entity A acquires Entity B.



**Focus on A's perspective**

## Observations

**Covered by BCUCC project, regardless** of whether the combining parties:

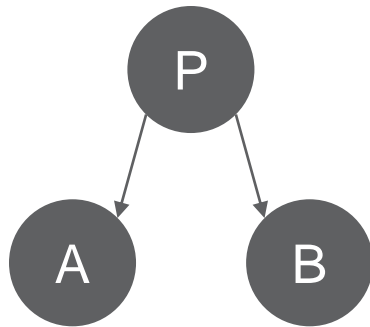
- are fully owned by Entity P or there is NCI in the combining parties;
- are listed or privately held; or
- are preparing for an IPO.



# Example 2—Newco

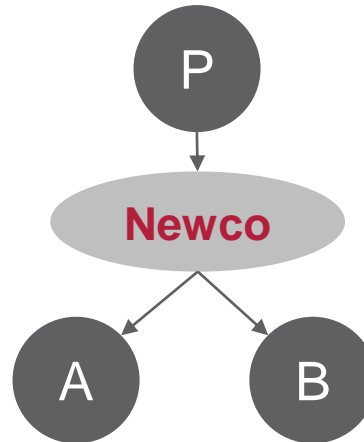
## Before

Entity A and Entity B are controlled by Entity P.  
Both Entity A and Entity B are businesses.



## After

Entity P forms a Newco and transfers Entity A and Entity B to that Newco.



**Focus on  
Newco's  
perspective**

## Observations

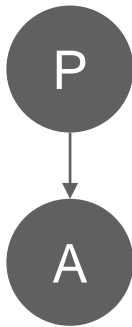
**Covered by BCUCC project, regardless** of whether:

- ✓ Newco can be identified as the 'acquirer' if IFRS 3 were applied to the transaction; and
- ✓ the combining parties:
  - are fully owned by Entity P or there is NCI in the combining parties;
  - are listed or privately held; or
  - are preparing for an IPO.

# Example 3—One business

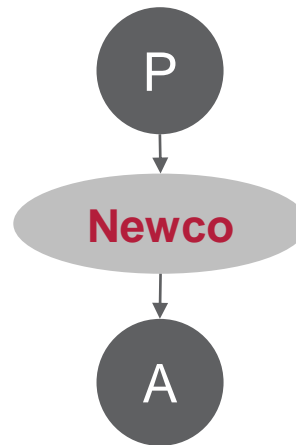
## Before

Entity A is controlled by Entity P.  
Entity A is a business.



## After

Entity P forms a Newco and transfers Entity A to that Newco.



**Focus on  
Newco's  
perspective**

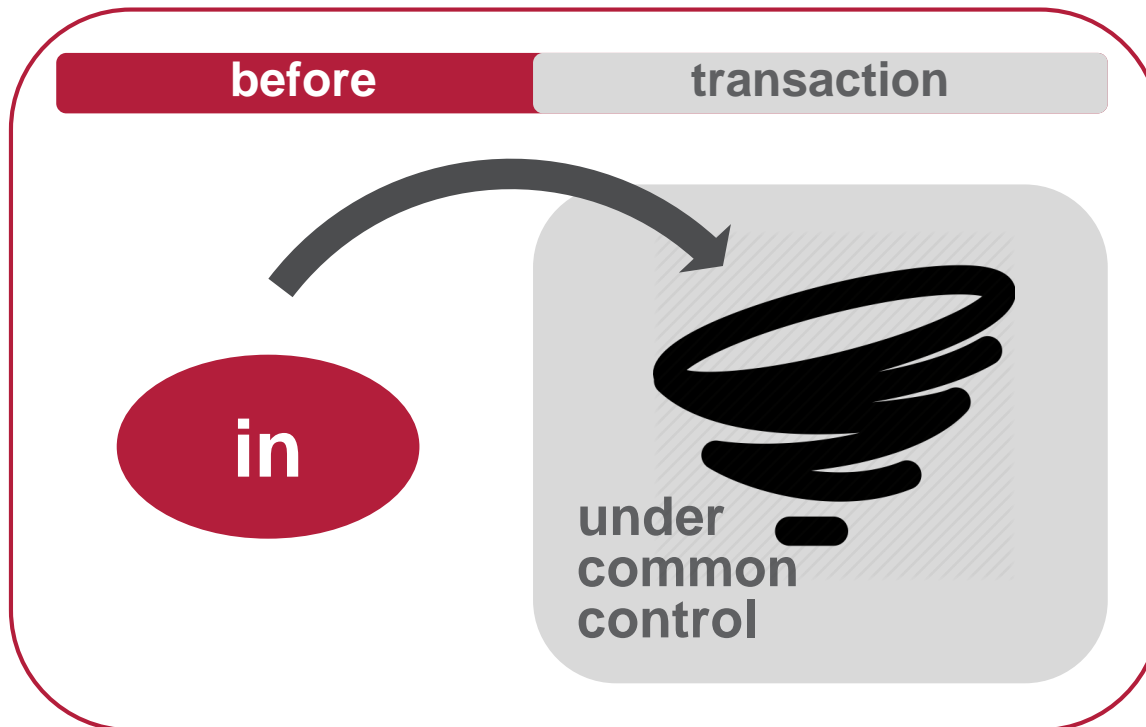
## Observations

**Covered by BCUCC project, regardless** of whether:

- ✓ Newco can be identified as the 'acquirer' if IFRS 3 were applied to the transaction; and
- ✓ the combining parties:
  - are fully owned by Entity P or there is NCI in the combining parties;
  - are listed or privately held; or
  - are preparing for an IPO.

# Transitory control—Situation A

## Staff recommendation



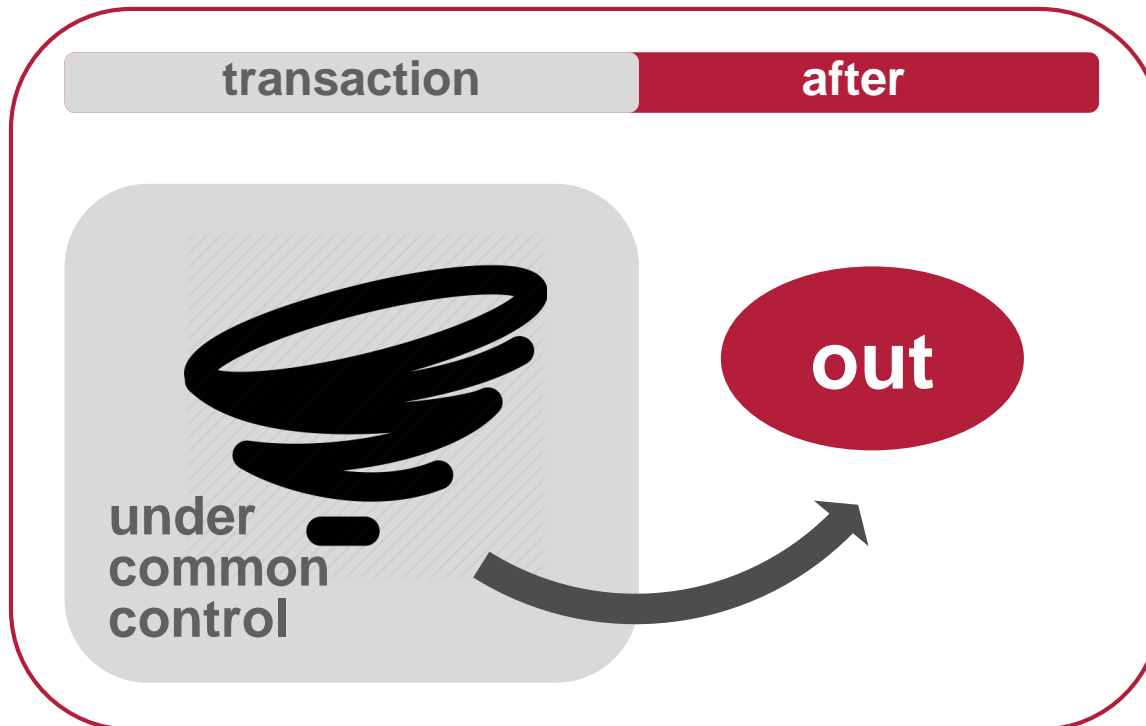
‘Fill in the gap’ in accounting for business combinations, instead of focusing on the distinction between BC and BCUCC



Transactions preceded by an external acquisition **will be covered by the BCUCC project**

# Transitory control—Situation B

## Staff recommendation



'Fill in the gap' in accounting for business combinations, instead of focusing on the distinction between BC and BCUCC



Transactions followed by an external sale, including those conditional on IPO, **will be covered by the BCUCC project**

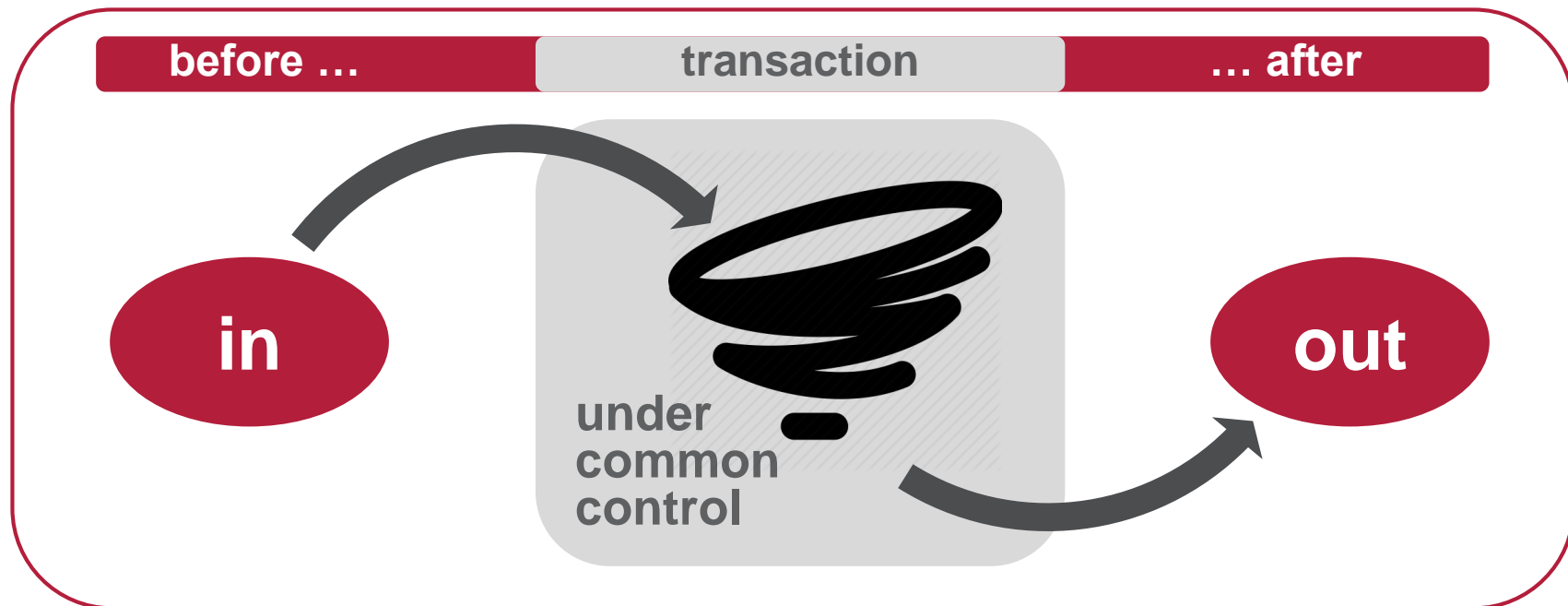
# Transitory control—Situation C

## Staff recommendation

‘Fill in the gap’ in accounting for business combinations,  
instead of focusing on the distinction between BC and BCUCC



Transactions preceded by an external acquisition *and* followed by an external sale  
**will be covered by the BCUCC project**





# Discussion

# Discussion



## Your views on the scope of the project

- Do you agree with the proposed scope of the project? If not, why?
- Are there any other transactions or perspectives that the Board should consider? If yes, what other transactions or perspectives and why?



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