

The opinion of the Polish Accounting Standards Committee (KSR) on the EFRAG and OIC Discussion Paper on Accounting for Business Combinations under Common Control (BCUCC)

*Accounting for Business Combinations under Common Control
Discussion Paper, October 2011*

1. KSR recognizes the importance of the BCUCC problem and its significance from the perspective of financial reporting practice which, in the current absence of appropriate solutions in IFRS, leads to diversity in approaches used and providing users of financial statements with information whose varied quality and distorted comparability contribute to financial statements being less useful. Therefore, an attempt to lay down the rules for accounting for BCUCC undertaken by EFRAG and OIC is appreciated by KSR and respected.
2. Due to their specific nature and the complexity of the situation in which they take place, BCUCC make a problem which raise numerous controversies as to the possibility of regulating them in a universal, uniform manner. The Discussion Paper identifies these problems and, in our opinion, constitutes a major contribution to the attempt to regulate the problem at the IFRS level.
3. However, KSR believes that seeing and solving the problem exclusively from the perspective of equity reorganizations and the reorganization of group structures, in BCUCC by looking at the effect of applying the solutions in the consolidated financial statements (CFS) of transferees being members of larger group structures, is too narrow. In other words, KSR is of the opinion that when searching for solutions for accounting for BCUCC, transactions of these types should be separated from those taking place at the ultimate group level. This is because BCUCC could relate to combinations in which control over the combining entities is in the hands of individuals (and entities) which do not prepare CFS or any other financial statements for general purposes. A separate analysis of the problem for these two BCUCC groups could eventually lead to identical conclusions but it could also lead to diverse conclusions, and adopting a uniform, universal solution could be inadequate.
4. In the practice of Polish businesses which apply IFRS, the group reorganizations covered by BCUCC and the Discussion Paper are usually accounted for applying the pooling-of-interests method. This is mainly due to the applicable Polish accounting regulations which puts one under the obligation to use such solutions (in the absence of IFRSs regulations). Such measures fall within the scope of the hierarchy of importance of the regulations set out in IAS 8. However, this does not mean that the Polish regulations as well as KSR provide exclusively for the pooling-of-interests method for BCUCC. This method is only indicated as one which is to be used. However, in no event the fresh start method considered in the Discussion Paper is practised, and it is hardly allowed. This method creates additional values which should not take place from the perspective of the CFS of the group in which BCUCC occurs. We do not see any justification for considering the possibility of applying this method as part of group reorganizations, since it cannot not be used even in traditional business combinations . The problem of accounting for BCUCC at the ultimate level of the group hierarchy, where the ultimate controlling party which is not an entity within the meaning of IFRS has decided to combine the entities which it controls, might look different. Therefore, when taking BCUCC into consideration, we think it important to separate the possibility of applying an appropriate method (appropriate methods) at transferee level, being the entity covered

in the Discussion Paper, and to analyze their appropriateness from the perspective of business combinations at a higher or the ultimate level.

5. From among the views presented in the Discussion Paper, from the perspective of the problem as a whole, KSR is most favourably inclined towards the third view which guarantees the possibility of complying, in justified BCUCC cases, with the provisions of IFRS 3, but which does not limit the application of other solutions. However, from the transferee's perspective, KSR is most favourably inclined towards the first view. Our approach to the diversification of solutions from the general perspective and a specific perspective has already been expressed above.
6. In analyzing the perspective of the transferee and the CFS prepared by it (also separate financial statements, when this involves a legal merger) taking over another business which may be a separate entity controlled so far by another entity in a given group, we should take it into account that the financial statements prepared by it serve the same purposes and should have the same quality characteristics as those of any other financial statements drawn up and presented for general purposes, which are referred to in IFRS. Therefore, from the perspective of the transferee it may be identified as the acquirer and, in these circumstances, there are no reasons why a full analogy to IFRS 3 could not be used, and the acquisition method should be applied. However, at this point we share the view presented in the Discussion Paper that applying the acquisition method in line with IFRS 3 to this type of BCUCC may mean the need to separately estimate, at a reliable level, the fair value of the consideration transferred and, if it is different, to recognize the difference between this value and the value arising from the acquisition contract as a transfer of resources to or from the ultimate parent. This is in line with variant one in view one. However, some of the KSR members share a view that is in line with variant two and even variant three. This stresses the fact that BCUCC are an unusually controversial issue for which final solution at the IFRS level will be a compromise of many different views and opinions. Seeing certain BCUCC as transactions in non-controlling interests which – in our opinion – have already remained practically at the level of the present IAS 27 (2008) and IFRS 10 (par. 30 of IAS 27 and par. 23 of IFRS 10) also remains to be considered.
7. Variant one in view one is backed up by the present IFRS solutions in which it is assumed that even when a business combination can be perceived by market participants as a true merger or a mergers of equals, such business combination should be recognized as an acquisition anyway, and the acquisition method should be used. Here, the acquirer must be specified without any exceptions, even when this is not obvious or there are serious doubts. But in a situation in which there is difficulty in specifying the fair value of the consideration transferred, it can be specified on the basis of the fair value of the transferred party.
8. However, using the acquisition method in full for accounting for BCUCC at the ultimate parent level raises serious doubts, all the more so because already in the present IFRS 3 solutions there is a qualification that the assets that are the subject of the consideration transferred, which are still controlled by the transferee, cannot be measured other than on the basis used so far (par. 38 of IFRS 3). Therefore, we see the need to analyze the BCUCC problem at various levels, as mentioned above.