

**Accounting for Business Combinations  
under Common Control**

**FEEDBACK STATEMENT**



OCTOBER

**2012**

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*The paper is issued jointly by the European Financial Reporting Advisory Group (EFRAG) and the Organismo Italiano di Contabilità (OIC).*

*The purpose of this feedback statement is to provide an overview of the key points made by respondents to the Discussion Paper 'Accounting for Business Combinations under Common Control' and to set out the responses of EFRAG and OIC to the issues raised by respondents. The broad range of respondents and the comprehensive nature of the comments received demonstrate the importance of, and interest in, this initiative.*

## Why EFRAG and OIC undertook the initiative

The Business Combinations under Common Control (BCUCC) project was initiated with a view to responding to concerns about the silence in the IFRS literature on this topic, and the resulting lack of clear consensus on how BCUCC transactions should be reflected in financial statements prepared under International Financial Reporting Standards (IFRS). EFRAG's and OIC's Discussion Paper '*Accounting for Business Combinations under Common Control*' (DP) represented the first step in their project to address those concerns.

The DP was open for comment until 30 April 2012. EFRAG, together with a number of National Standard Setters, also organised a total of four outreach events on the subject in Europe. The feedback received at those events, which was in line with the responses summarised in this document, has been reported separately both in a detailed and in a consolidated format. All these reports are available on EFRAG's website ([www.efrag.org](http://www.efrag.org)).

## Proactive Work in Europe

EFRAG aims to influence future standard setting developments by engaging with European constituents and providing timely and effective input to early phases of the IASB's work. This proactive work is supported by a number of standard-setters in Europe to ensure resources are used efficiently and to promote stronger coordination at the European level.

The four strategic aims that underpin EFRAG's proactive work are:

- To engage with European constituents to ensure we understand their issues and how financial reporting affects them.
- To influence the development of global financial reporting standards.
- To provide thought leadership in developing the principles and practices that underpin financial reporting.
- To promote solutions that improve the quality of information, are practical, and enhance transparency and accountability.

More detailed information about our proactive work and current projects is available on EFRAG's website ([www.efrag.org](http://www.efrag.org)).

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# Executive Summary

## OBJECTIVE

- 1 EFRAG and the Italian Standard Setter the Organismo Italiano di Contabilità (OIC) started their project on Business Combinations under Common Control (BCUCC) to address concerns about the lack of guidance in the IFRS literature on how to account for BCUCC in both consolidated and separate financial statements prepared under IFRS.
- 2 In October 2011, EFRAG and OIC issued the Discussion Paper '*Business Combinations under Common Control*' (DP) for public consultation. The scope of this DP was limited to considering BCUCC in consolidated financial statements and represents EFRAG's and OIC's first step in their BCUCC project.
- 3 The objective of the DP was to set the scene and to stimulate the debate on BCUCC at an early stage in the standard setting process, before the IASB formally issued a proposal on how to account for these transactions. EFRAG asked for comments on the proposals in the DP to arrive no later than 30 April 2012.
- 4 During April and May 2012, to support the publication of the DP, to increase the level of response to it, and to further stimulate debate, EFRAG, together with a number of National Standard Setters, organised several events in Europe to discuss the subject. The key themes raised in those events, which are summarised in a separate consolidated feedback statement, were in line with the responses reflected in this document.

## PROCESS

- 5 After receiving the comments on the DP, the project team analysed the comment letters and presented their findings to EFRAG and OIC. These findings have formed the basis of the project team's recommendations on how to move ahead.
- 6 The objective of this Feedback Statement is for constituents to consider the analysis of comment letters received, together with EFRAG's and OIC's responses to the issues raised by respondents. It will also provide a context for constituents to understand the underlying reasons for the way EFRAG and OIC have decided to develop the project.

## LEVEL OF RESPONSE TO THE DP

- 7 EFRAG received 28 comment letters to the DP (including 18 comment letters from European constituencies).
- 8 The comment letters were mainly submitted by accounting bodies, National Standard Setters and business associations, with a smaller number being received from individual companies.
- 9 The following table shows the total number of respondents to the DP and provides a high level overview of the respondents' details, including the type of respondent and country of operation:

	Europe											The Rest of the World				Global	Total			
	NL	DK	FR	SW	BE	NO	AT	GB	IT	PT	PL	EU	AU	SA	CA			Korea		
Accounting bodies				1				3						1						5
Standard Setters	1		1		1	1		1		1	1		1		1	1				10
Standard-Setters and Accounting Bodies		1																		1
Preparers							1		1											2
Accounting Firms																			7	7
Regulatory Bodies												1								1
Professional Associations							1		1											2
<b>Total</b>	<b>1</b>	<b>1</b>	<b>1</b>	<b>1</b>	<b>1</b>	<b>1</b>	<b>2</b>	<b>4</b>	<b>2</b>	<b>1</b>	<b>1</b>	<b>1</b>	<b>1</b>	<b>1</b>	<b>1</b>	<b>1</b>	<b>1</b>	<b>7</b>	<b>28</b>	

- 10 Most of the respondents welcomed the DP as an introduction to an important debate.
- 11 Eighteen comment letters provided support for the project and some of the analysis in the DP.
- 12 Seven respondents did not express their overall support for the analysis and views presented in the DP, but nevertheless agreed that the topic is important and that a debate on how to account for BCUCC is needed.
- 13 Although supporting the project, three respondents expressed concern about the analysis in the DP, or with the decision-usefulness in practice of the application of IFRS 3 *Business Combinations* to the subject.

## MAIN ISSUES RAISED BY RESPONDENTS

- 14 The main issues raised by the respondents relate to the following areas:
- *Objective of the DP*
  - *Scope of the DP*
  - *Real life examples*
  - *Definition of BCUCC*
  - *Approach taken in the DP*
  - *User needs*
  - *Accounting approaches for BCUCC*
  - *Diversity in practice*
  - *Economic substance of BCUCC transactions.*
- 15 The comments indicated that there are mixed views on whether the DP achieved all of its objectives. Although there was agreement about the DP stimulating debate on BCUCC, some respondents commented that the objectives would have been better achieved if the scope of the DP had been wider.
- 16 A number of respondents noted that the scope of the DP was too narrow and, as a consequence, additional issues should have been considered. In particular, these respondents' view was that the DP should have considered other types of transactions under common control (e.g. Initial Public Offerings, newco formations, hive ups, legal mergers and demergers). Without a consideration of the wide variety of similar operations, the respondents deemed the DP to be incomplete.
- 17 Respondents also expressed the view that the project should include in its scope how to account for BCUCC in the separate financial statements.
- 18 Many respondents stated that the project's effective development would be greatly aided by considering real-life examples of BCUCC.

- 19 Most respondents asked for a common definition of BCUCC transactions to be provided.
- 20 Mixed views were expressed about the approach taken in the DP. Some supported the approach taken. Others expressed the view that the hierarchy approach followed in the DP (based upon IAS 8 *Accounting policies, changes in accounting estimates and errors*) inappropriately limited the analysis to the current IFRS literature, rather than taking it as a starting point. These respondents suggest that EFRAG should have reflected on different types of transactions, the Conceptual Framework and user needs.
- 21 The majority agreed that the information needs of users are an important consideration when determining an accounting method for BCUCC. They also commented that ultimately, the method used to account for BCUCC transactions should be capable of satisfying the needs of users. However, a number of respondents stated that more work needs to be done to address the information needs of users on BCUCC transactions.
- 22 Regarding the accounting methods used in practice, almost all respondents noted that either predecessor or acquisition accounting are prevalent. Many respondents highlighted the need to consider the substance of the transaction. The responses also indicated that the use of fresh start accounting is very limited and is the least preferred method in practice. However, a number of respondents took the alternative view that the DP should have considered accounting treatments currently outside the boundaries of IFRS requirements.
- 23 Generally respondents supported diversity of accounting treatment when facts and circumstances merit it. They commented that the factors underlying such diversity and the consequences of diverse treatment should be explored further. It was a common view that whatever method is chosen, it should be applied consistently.
- 24 Some respondents held the view that the economic substance of BCUCC transactions should determine the accounting method and the recognition of certain items as part of equity. They pointed out that similar BCUCC transactions can have different economic substance, which might be a reason for the diversity in practice. Some respondents went further and suggested exploring what constitutes economic or commercial substance; for example, the development of a list of indicators to ensure that the accounting approach chosen results in information relevant to users.

# Summary of responses of EFRAG and OIC

- 25 The discussion below includes the responses of EFRAG and OIC to the main issues raised by constituents and gives an indication of the agreed direction of the future development of the project.

## Objective of the DP

- 26 The DP has started the debate about how to account for BCUCC, and to this extent the objective of the DP has been fulfilled. However, some respondents questioned whether the remainder of the objective of the DP has been achieved.

### EFRAG and OIC response

- 27 We believe the DP achieved part of its objective which was to stimulate debate. The DP is only the first step in the EFRAG's and OIC's overall project on BCUCC. Therefore, we agree that more work should be considered to achieve the objective of the overall project and the DP in particular.

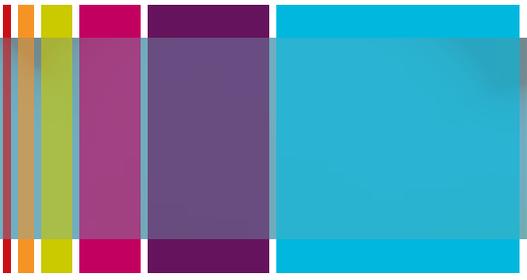
## Scope of the DP

- 28 The DP's scope was too narrowly defined.

### EFRAG and OIC response

- 29 We understand the view that a possible logical starting point for the DP would have been a discussion of the accounting principles to be applied to common control transactions in general. However, the DP is only the first step in the overall project on BCUCC which was undertaken by EFRAG and OIC because there is no guidance for BCUCC in IFRS. As a first step, the scope of the DP was limited to considering BCUCC in the consolidated financial statements. If the scope of the DP had been widened, EFRAG and OIC might have included other areas as suggested by respondents, such as the accounting for BCUCC in the separate financial statements.

- 30 Concerning the accounting treatment in separate financial statements, this aspect was carefully considered in framing the overall project on BCUCC. When developing the DP, EFRAG and OIC concluded that it was not feasible to address adequately all the issues involved with accounting for BCUCC in the separate financial statements at that stage. However, given its significance, EFRAG and OIC invited constituents to comment specifically on this issue in the DP. The feedback received from respondents on this question will be used in the ongoing project '*Separate financial statements*'. In this project EFRAG, together with OIC, the National Standard Setters of Netherlands (DASB) and Spain (ICAC) will analyse possible accounting requirements for BCUCC in the separate financial statements, and also consider the issues arising from the overall application of IFRS to separate financial statements.



In particular, the scope of the work on ‘*Separate financial statements*’ encompasses common control transactions and so this project offers a wider scope than the DP. Common control transactions are a wide and difficult area which needs careful consideration before starting the work.

## Real life examples

- 31 Many respondents suggested that EFRAG and OIC should consider real-life examples in determining possible principles for accounting for BCUCC transactions.

### EFRAG and OIC response

- 32 Further work on the project will focus on analysing real-life examples to help characterise differences in the underlying facts and circumstances in the variety of BCUCC that actually take place. The project team will begin gathering real-life examples from those respondents that made such a recommendation or referred to real-life examples in their comment letters. Once received, we will try to identify discriminating characteristics and see whether these examples can be analysed in a manner that provides a framework helpful in identifying the different types of BCUCC transaction that actually take place.
- 33 In addition, the project team intends to use the information gathered through the real-life examples to try to define BCUCC, since this is an area where respondents suggested that some clarification was needed.
- 34 Consideration of real-life examples might prove that diversity in practice exists and also increase EFRAG’s and OIC’s understanding of the issues that constituents have raised about BCUCC. However, we note that the project team have stated that developing the project in this way might be challenging, in particular if constituents regard it as an effective means to solve the various accounting issues related to BCUCC. For example, information about real-life BCUCC transactions may be limited, or may not cover the broad range of different BCUCC transactions that can occur. Furthermore, all the facts and circumstances necessary to assess the accounting method chosen for a real-life BCUCC transaction may not be available.

## Definition of BCUCC

- 35 Most respondents asked for a common definition of BCUCC transactions.

### EFRAG and OIC response

- 36 EFRAG and OIC agree that future work on the overall BCUCC project should consider framing a definition of BCUCC transactions, since this is an essential step in developing a common understanding of the type of transactions that are under consideration.

37 Therefore further work in the project will consider the definition of BCUCC transactions. Consequently, when asking respondents for real-life examples, the project team will also ask whether they have developed a definition of BCUCC within their organizations and, if so, what the definition is.

38 The project team may also consider field-testing the definition of BCUCC once it is developed.

## Approach taken in the DP

39 Some respondents indicated that the use of the IAS 8 hierarchy adversely limited the approach and the analysis contained within the DP.

### EFRAG and OIC response

40 EFRAG and OIC formulate the comments below.

41 The rationale for issuing the DP was to assist in filling the gap in IFRS concerning BCUCC transactions. As a consequence this entailed working within the IFRS context. Therefore it followed that the DP should apply the IAS 8 hierarchy and first look for IFRSs dealing with similar and related issues, which is the procedure IAS 8 prescribes in the absence of an applicable IFRS. This approach was also supported by the fact that there is no basis for conclusions justifying, on technical grounds, the decision to exclude BCUCC from the scope of IFRS 3.

42 The approach taken in the DP also considered the Conceptual Framework, which according to the IAS 8 hierarchy should also be referred to when developing an accounting policy in the absence of an applicable IFRS.

43 The fresh start method, which is not part of IFRS, is considered in the DP. This shows that the approach in the DP was not rigidly constrained by the current requirements of IFRS.

44 Overall, EFRAG and OIC take the view that their analysis in the DP has not been unduly limited.

45 However, EFRAG and OIC understand that those who might want to consider common control transactions in a comprehensive and completely unconstrained manner may disagree with the IAS 8 hierarchy approach.

## User needs

- 46 Some respondents pointed out that more work needs to be done to identify and address the information needs of users on BCUCC.

### EFRAG and OIC response

- 47 EFRAG and OIC believe the DP includes a reasonable discussion on the information needs of users, for example when discussing View 3 in the DP that suggests the analogy to IFRS 3 may apply. However, we accept that some of the comments made by respondents may need to be addressed as part of the proactive project on *'Separate financial statements'*.

## Accounting approaches for BCUCC

- 48 Almost all respondents indicated that either predecessor or acquisition accounting is used in practice rather than fresh start accounting.

### EFRAG and OIC response

- 49 We do not see any need further to explore fresh start accounting at this stage of the project; however, this accounting method might be considered by the IASB when it continues its research on BCUCC transactions.

## Diversity in practice

- 50 Most respondents expressed the view that diversity of practice in accounting for BCUCC is not necessarily undesirable. Some suggested that further analysis of the factors underlying such diversity, and the consequences of it, would be beneficial.

### EFRAG and OIC response

- 51 To some extent the DP may have lacked clarity around the notion of diversity, because the DP is intended to have referred to this notion when discussing different accounting for similar transactions. Views 1 and 2 in the DP that suggest one single accounting treatment for all BCUCC may have triggered this comment. We agree with constituents that where diversity reflects different economic underlying facts and circumstances, different accounting treatments, appropriately depicting such differences, would be highly desirable.
- 52 In addition, EFRAG and OIC believe that considering real-life examples, as explained above, might help increase our understanding of the factors underlying diversity of accounting treatments.

## Economic substance of BCUCC transactions

- 53 Some respondents suggested developing a list of indicators to help identify the economic or commercial substance of BCUCC transactions.

### EFRAG and OIC response

- 54 The DP includes (in appendix 3) a summary of the discriminating factors that were provided by the project team in formulating View 3. Generally, this approach did not attract much support from respondents. However, the responses received indicated some interest in re-visiting this type of approach in the future.
- 55 This is a matter that the project team might consider exploring, depending upon the outcome of the analysis of the real-life examples. Therefore, EFRAG and OIC will decide at a later stage whether or not to proceed with this suggestion.

# Summary of detailed comments provided by respondents

- 56 The following paragraphs include a summary of the detailed comments provided by respondents in support of the main issues they raised, as set out in the Executive Summary. A number of other issues respondents raised are also included in the discussion below.
- 57 EFRAG and OIC have not provided specific responses to the detailed comments made by respondents in support of the main issues they raised. Our views on the substantive issues are already summarised in the previous section.

## Scope of the DP

- 58 Some respondents noted that the accounting treatment for BCUCC is closely linked to certain other accounting issues and should not be considered in isolation. Therefore, these respondents suggested additional areas for consideration as part of the project scope in order to include all the issues pertinent to accounting for BCUCC. There were two main areas suggested by respondents:
- (a) Accounting for BCUCC in the separate and individual financial statements. This area is important since (i) dividends are distributed based on these financial statements, and (ii) the majority of subgroups in Europe are exempted from preparing consolidated accounts if these are prepared by an ultimate or intermediate parent; and
  - (b) Common control transactions other than BCUCC, since a number of issues raised in the DP might also be relevant for common control transactions in general (for example, transfer of a group of assets that do not constitute a business, reorganisations within a group that do not constitute business combinations, and sales of inventory, fixed assets and provision of management services). In this regard, some respondents noted that it is important to explain conceptually why business combinations that occur between entities under common control might be subject to different accounting treatment than other common control transactions.
- 59 Respondents also indicated additional areas and some specific issues which they would like to be explored, even though they fall partly outside the scope of the project:

### Additional areas

- (a) Accounting in the financial statements of the transferor;
- (b) The effect of BCUCC transactions on any non-controlling interests; and
- (c) Defining whether and when it is appropriate to restate comparatives for BCUCC transactions.

## Specific issues

- (d) Cost, and what is meant by cost, of the investment which needs to be eliminated on consolidation;
  - (e) Transactions in the form of hive-ups to a parent of a business or of assets, in particular the accounting entries that may arise in the transferor's and transferee's separate financial statements. This type of transaction needs to be considered, because they may be undertaken for a nil consideration. Under these circumstances, if the assets received are recorded at fair value, there is a question over how the resulting credit to equity should be designated in the transferee's separate financial statements.
  - (f) Transactions involving newly incorporated companies within a group (newco formations), since these transactions do not usually involve the combination of businesses but might raise similar problems to BCUCC;
  - (g) Which entity's book values should be used when applying the predecessor accounting approach, since book values in the individual accounts of the transferred entity may differ from those used by the group for consolidation purposes;
  - (h) Reconsideration of the issues contemplated by IFRS 17 *Distributions of Non-cash Assets to Owners*; and
  - (i) Entity combination reporting in cases where there is no significant shift in control arrangements.
- 60 Some respondents suggested developing indicators which could provide guidance about the most appropriate method of accounting for BCUCC in given circumstances. The DP considered some indicators in formulating View 3, however, these respondents would like EFRAG and OIC further to explore this approach.
- 61 One respondent noted that the issue of BCUCC transactions is also important for the public sector and the wider non-profit sector, since a large number of the combinations done in the past in both sectors have been under common control.

## Definition of BCUCC

- 62 Most respondents stated that a definition of BCUCC is necessary to clarify the type of transactions included in the scope of the DP. Without a clear definition, the impact of the discussion in the DP can be misinterpreted, as it may have a different meaning for different readers.
- 63 It was noted by one respondent that many would expect the project to include a consideration of common control established through state ownership.

## Approach taken in the DP

- 64 Those respondents that did not support the IAS 8 hierarchy as the starting point for developing an appropriate accounting method for BCUCC transactions provided the following reasons:
- (a) The use of the IAS 8 hierarchy might have given undue importance to IFRS 3 compared with other alternatives; and
  - (b) Not all of the approaches documented in the DP are appropriate interpretations of IAS 8 and current IFRS.
- 65 Some respondents would have favoured an approach starting first with the Conceptual Framework and developing a new principles-based approach from there. This is because, in their view, the current silence on BCUCC in the IFRS literature is indicative of the complexity of the issue, thus innovation may be needed to produce high quality financial reporting requirements. Some respondents further indicated that only if the nature of the transactions differed should the accounting treatment differ.
- 66 Other respondents stated that a consideration of the existing guidance in national GAAPs would have been welcome in the analysis. These respondents encourage EFRAG and OIC to conduct a thorough review of existing guidance in accounting frameworks and literature to identify approaches and key concepts that should be considered.
- 67 From a more general perspective, some respondents commented that the DP should inform IASB about the issues faced in practice, rather than trying to find solutions to the problems of accounting for BCUCC transactions. Others noted that resolving BCUCC accounting issues should not be driven by specific regulatory needs.

## BCUCC and the perspective to be taken

- 68 The analysis in the DP looked at financial reporting from the perspective of the transferee, consistent with the entity, rather than the proprietary perspective.
- 69 Many respondents providing comments on this matter agreed that the entity perspective should be dominant. However, some pointed out that aspects of the proprietary perspective still exist within IFRS. Others provided the general comment that the approach applied should not negatively influence the information provided, and that the role of the controlling shareholder should not be ignored in determining an appropriate accounting model.

## User needs

- 70 Respondents overall agreed that any accounting method for BCUCC should be capable of satisfying the needs of users; however, they provided different views on this issue. Some respondents suggested that users would be well-served by practical improvements to the consistency, understandability and transparency of reporting BCUCC. One respondent noted that disclosure requirements on accounting policy and management judgement could play an important role in this area.
- 71 Other respondents observed that users are a diverse group and not all users have the same needs, therefore it is unlikely that a single approach would accommodate all users' needs. An important consideration is whether the needs of users of consolidated and individual entity accounts differ in the context of BCUCC. Undertaking further research on user needs for different categories of BCUCC might provide insights into whether the selection of a BCUCC accounting method should be a free choice or be addressed by authoritative guidance. In considering the needs of users, the cost of each alternative and the benefits to be derived should be considered.

## Accounting approaches for BCUCC

- 72 Most respondents are of the view that there should be different approaches depending on the nature of the BCUCC, since in certain cases acquisition accounting would be more suitable, whereas in other cases either predecessor accounting, or the 'fresh start' model, would provide more useful information. In determining which approach would be appropriate, the 'change in ability'<sup>1</sup> model in the DP seems to be relevant in making the judgements involved; but there may also be other indicators that should be considered.
- 73 A number of respondents took the view that the DP did not sufficiently consider whether the accounting for BCUCC should reflect the economic substance and nature of the transaction concerned. Others stated that further consideration should be given to developing a range of indicators to help identify the commercial substance of a transaction, thereby ensuring the accounting treatment adopted results in useful information. (This is further commented on under the separate heading '*Economic substance of BCUCC transactions*'.) These respondents noted that the use of indicators would be consistent with the approach taken in some jurisdictions in developing local accounting requirements.
- 74 Respondents were not in favour of imposing an unduly restrictive approach that would restrict the viable accounting alternatives, since it could reduce the usefulness of information for users. It was nevertheless a common comment that whatever method was chosen, it should be applied consistently.

<sup>1</sup> According to the DP the 'change in ability' model considers whether there has been a change in the ability of the entity to meet the claims of the capital providers against the combining entities that existed prior to the BCUCC.

- 75 A few other respondents disagreed with the accounting approaches included in the DP in general. One respondent stated that no practical solutions are identified in the DP, which in turn limits the debate about possible solutions. This respondent's view was that the proposals in the DP were not properly justified as none of them was linked to the features of the transactions being analysed in it. Further, this respondent considered that the DP did not analyse the issues faced by practitioners, instead only giving a list of alternative views. Another respondent stated that the evidence presented in the DP was not sufficiently well developed to allow a workable solution to be based upon it. The general disagreement of these few respondents stemmed from their rejection of the IAS 8 hierarchy approach.

### Acquisition accounting

- 76 Some respondents disagreed with the importance given by the DP to IFRS 3 when considering accounting approaches to BCUCC transactions. This was because they interpreted the exclusion of BCUCC from its scope as an indication that IFRS 3 could have no bearing on the matter. These respondents also noted that applying IFRS 3 to BCUCC transactions might be difficult because an acquirer is not always identifiable and BCUCC transactions might not be transacted at arm's-length value. The disagreement with the use of acquisition accounting also stems from the rejection of the IAS 8 hierarchy approach.
- 77 A number of respondents preferred the application of acquisition accounting when the transaction has economic substance. Although in some cases it might be difficult to apply IFRS 3 by analogy, the adoption of this method could be justified by the necessity to reflect the economic substance of the BCUCC transaction. This is because the acquisition method results in a reassessment of the value of the net assets of one or more of the entities involved and/or the recognition of goodwill and intangible assets. According to these respondents, acquisition accounting might provide useful information if ownership interests have changed; for example, when (i) new owners have been brought in, (ii) proportionate interests in the combining entities have changed or (iii) non-controlling interests are affected, and the transaction price is not at fair value. It might also provide useful information for those BCUCC transactions where the purpose is to establish the basis for a sale of the business to an external party. Further, some of these respondents noted that if an analogy to IFRS 3 is valid, then all the requirements of IFRS 3 should apply.
- 78 Those respondents that did not support the application of acquisition accounting to BCUCC noted that:
- (a) BCUCC and ordinary business combinations are different in nature. In addition, BCUCC are transactions that occur in a great variety of forms; therefore there might be cases where the application of acquisition accounting does not produce useful information for users. Consequently it might be appropriate to consider a different measurement basis rather than trying to scope all BCUCC transactions into IFRS 3 by analogy. For example, this might apply to reorganisations within a consolidated group where there is no change in the economic position of the group, and to combinations where there may be a common controlling individual who does not prepare consolidated accounts;

- (b) A market based valuation cannot always be simulated (there are too many variables and valuation is subjective). In addition, it was suggested that where such a valuation could be done, its use could lead to non-comparable results. Thus, further research should be conducted on this matter;
- (c) The use of acquisition accounting in all circumstances could create restructuring opportunities for groups, since entities might recognise income in profit or loss by changing ownership within the same ultimate legal entity; and
- (d) If there is no economic substance to the BCUCC and the business combination is undertaken solely for the controlling parent's purposes, then the costs of making the required fair value measurements of both entities can exceed the benefits of making those measurements.

### Predecessor accounting

- 79 A number of respondents were in favour of using the predecessor basis if the BCUCC has no or only a limited influence on the economic situation of the group. They took the view that the predecessor basis of accounting properly portrays the fact that there has been no change in control. In addition, they suggested applying this method to specific circumstances such as when (i) BCUCC transactions involve wholly owned entities, and (ii) existing owners have simply reorganised their existing ownership interests; for example, to achieve tax advantages or other synergies.
- 80 According to some respondents, there are additional issues to be considered when choosing between acquisition and predecessor accounting. Such issues might include whether both approaches should be permitted as a 'free' accounting policy choice or alternatively, whether entities should be required to apply one or the other in particular circumstances. Some respondents supported analysing practical examples on the application of each method.
- 81 However, other respondents highlighted particular difficulties with both approaches. If acquisition accounting is used to account for BCUCC transactions, the main problems are to identify the acquirer, and to agree on a uniform accounting treatment when the consideration transferred differs from the fair value of the business acquired. There might be also the risk of recognising some assets, such as internally generated intangibles and goodwill on BCUCC transactions, that may be deemed to lack economic substance. In addition, for substantive transactions, a number of respondents pointed out that this type of asset might be difficult to measure reliably. Regarding predecessor accounting, respondents noted that this method has been applied in different ways, resulting to other difficulties such as: (i) determining the predecessor value, (ii) the recognition of goodwill, and (iii) the basis for recognising items such as intangible assets and contingent liabilities.

## Fresh start

- 82 A few respondents suggested applying the fresh start accounting approach in those situations where the economic substance was other than that of a group reorganisation.

## Diversity in practice

- 83 Some respondents noted that diversity in practice also exists for other common control transactions such as transfer of assets, and suggested developing guidance on these transactions, including “not arms’ length” transactions.

## Economic substance of BCUCC transactions

- 84 In general, respondents argued that if the substance of the transaction is considered, the information needs of users will be met. The aim being to avoid representing a change in economic substance when, in fact, there is none.

- 85 Developing a set of indicators of economic substance might be important for deciding the most appropriate accounting method, since it would help to identify which indicators need to be present for a particular accounting method to be applied, or to state under which circumstances there might be a free choice of accounting policy. For example, one respondent suggested considering the following factors when evaluating whether a BCUCC transaction has economic substance:

- (a) Purpose of the transaction;
- (b) Involvement of outside parties in the transaction;
- (c) Whether or not the transaction is conducted at fair value;
- (d) Existing activities of the entities involved in the transaction;
- (e) Whether a reporting entity is bringing entities together that did not exist before; and
- (f) Where a new company is established, whether it is undertaken in connection with an IPO or spin-off or other change in control and significant change in ownership.

- 86 Some respondents supported developing a set of indicators to distinguish BCUCC from other business combinations that exist in practice, before any consideration is given to the appropriate accounting treatment for BCUCC. Others preferred a principles-based approach rather than following a simple diagram like the one in the DP, or using a list of indicators.

- 87 Other respondents suggested that a definition of economic substance should be developed, thereby allowing two types of accounting treatment for BCUCC: one for those transactions having economic substance; and one for those that have not. Such solution might be consistent with the approach used in current IFRS literature to account for other transactions.

## Disclosures

- 88 A number of respondents indicated that there are specific disclosure issues to be addressed for BCUCC. Some respondents recommended that IAS 24 *Related Party Transactions* should be used as a basis for developing relevant disclosures. Others referred to the requirements of IFRS 3 and suggested that the relevant paragraphs of this standard should be included as part of the disclosure requirements. Also respondents indicated that disclosures should be required about the accounting approach used, the judgments applied, and the principal assumptions used.
- 89 It was a common suggestion that disclosures are an issue that should not be dealt with until an accounting method for BCUCC transactions has been agreed.

# Appendix 1

## List of Respondents

<i>Type of respondent</i>	<i>Name of respondent</i>	<i>Location</i>
<i>Accounting bodies</i>	Association of Chartered Certified Accountants	Global
	Chartered Institute of Public Finance and Accountancy	UK
	Institute for the Accountancy Profession in Sweden	Sweden
	Institute of Chartered Accountants in England and Wales	Global
	South African Institute of Chartered Accountants	South Africa
<i>Accounting firms</i>	BDO	Global
	Deloitte	Global
	Ernst & Young	Global
	Grant Thornton	Global
	KPMG	Global
	Mazars	Global
	PwC	Global
<i>Preparers</i>	Abfall Services AG	Austria
	Luxottica	Italy
<i>Professional associations</i>	Austrian Financial Reporting and Accounting Committee	Austria
	Group of Certified Italian Accountants in Rome	Italy
<i>Regulators</i>	European Securities and Markets Authority	Europe
<i>Standard Setters</i>	Accounting Standard Board staff	Canada
	Dutch Accounting Standard Board	The Netherlands
	Australian Accounting Standards Board staff	Australia
	Norsk Regnskapsstiftelse	Norway
	Korean Accounting Standards Board staff	Korea
	The United Kingdom Accounting Standards Board	UK
	Autorité des normes comptables	France
	Polish Accounting Standards Committee	Poland
	Belgian Accounting Standards Board	Belgium
	Comissão de Normalização Contabilística	Portugal
<i>Standard Setters and accounting bodies</i>	Danske Revisorer – FSR	Denmark

